S T A T E   O F   M I C H I G A N

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of **CONSUMERS ENERGY COMPANY** for authority to increase its rates for the distribution of natural gas and for other relief.	)	Case No. U-18124

At the July 31, 2017 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. Sally A. Talberg, Chairman
Hon. Norman J. Saari, Commissioner
Hon. Rachael A. Eubanks, Commissioner

ORDER

I. HISTORY OF PROCEEDINGS

On August 1, 2016, Consumers Energy Company (Consumers) filed an application seeking authority to increase rates, amend its rate schedules, obtain approval of certain accounting matters, and modify certain terms and conditions of providing natural gas service. Consumers indicated in its application that, based on a projected test year commencing January 1, 2017, and ending December 31, 2017, the company expected to experience a revenue deficiency of $90.483 million annually.

A prehearing conference was held on September 14, 2016, before Administrative Law Judge Suzanne D. Sonneborn (ALJ). At the prehearing conference, the ALJ granted petitions for leave to intervene filed by the Association of Businesses Advocating Tariff Equity (ABATE) and the

Michigan Department of the Attorney General (Attorney General). Intervention was subsequently granted by written ruling to the Midland Cogeneration Venture Limited Partnership (MCV).[1] The Commission Staff (Staff) also participated in the proceedings.

On December 14, 2016, Consumers filed testimony and exhibits notifying the Commission that the company intended to self-implement a $60 million rate increase commencing January 29, 2017, to be allocated based on the statutorily-mandated equal percentage basis. MCL 460.6a(1). On January 20, 2017, the Commission issued an order in this case finding good cause to deny any self-implemented rate increase in excess of $20 million. Consumers self-implemented a rate increase of $20 million on January 29, 2017.

On December 19, 2016, the Staff filed its direct testimony and exhibits, and on December 22, 2016, ABATE and the Attorney General filed testimony and exhibits. On January 20, 2017, Consumers, the Staff, ABATE, and the Attorney General filed rebuttal testimony and exhibits. Evidentiary hearings were held on February 8-10, and 13, 2017. Initial and reply briefs were filed by Consumers, the Staff, ABATE, and the Attorney General.

The ALJ issued a Proposal for Decision (PFD) on May 18, 2017. Consumers, the Staff, ABATE, and the Attorney General filed exceptions on June 8, 2017, and replies to exceptions on June 19, 2017. The record consists of 1,885 pages of transcript and 271 exhibits.[2]

II. LEGAL STANDARDS

In exceptions and replies to exceptions, the Attorney General presented, for the first time, arguments concerning the legal standard applied by Consumers. He states that the company

[1] MCV did not thereafter participate.

[2] In this order, the Commission addresses the issues in roughly the same sequence in which they were addressed in the PFD.

"seemingly ignores the legal standards that apply in general rate cases before the Commission and that it has the burden of substantiating and proving its proposals are reasonable and prudent." Attorney General's replies to exceptions, p. 3. The Attorney General asserts that Consumers' burden of proof is a preponderance of the evidence. He argues, "Even if Consumers presents substantial evidence on an issue, that alone does not require the Commission to rule in its favor." *Id.*, p. 5. Therefore, the Attorney General requests that the Commission keep these "burdens and obligations" in mind when reviewing the company's requests. *Id*.

In reply, Consumers argues that it has met the proper burden of proof for all of the issues in this case and has provided full evidentiary support for its requested rate relief.

The ALJ did not address this issue. The Commission is mindful of the Attorney General's arguments and concerns, and notes that these issues were fully addressed in the January 31, 2017 order in Case No. U-18014 (January 31 order), pp. 8-9; the September 8, 2016 order in Case No. U-17895, p. 4; and the January 11, 2010 order in Case No. U-15768 *et al.*, pp. 9-10.

III. TEST YEAR

Consumers proposed using calendar year 2017 as the projected test year and 2015 as the historical year. ABATE objected because Michigan law does not require the use of a projected test year, and the company's evidentiary presentation comparing its historical year to its projected test year shows that Consumers over-earned on an historical basis, both in terms of dollars and authorized return on equity (ROE).

Consumers responded that ABATE's request for an historical test year is inconsistent with MCL 460.6a(1). Consumers argued that ABATE provided no evidence to support its claim that these alleged periods of over-earning should reduce rates in a projected test year. In addition, Consumers stated that, for the first time in its initial brief, ABATE claimed that the company over-earned its authorized ROE in 2016 and in the projected 2017 test year, but that ABATE presented no evidence to support this claim.

The ALJ agreed with Consumers that ABATE's request for use of an historical test year should be rejected. The ALJ stated that MCL 460.6a(1) "clearly permits the Company to have its rates based on a projected test year." PFD, p. 9. In addition, the ALJ quoted page 9 of the January 11, 2010 order in Case Nos. U-15768 and U-15751, wherein the Commission affirmed that a utility may use a projected test year to develop its requested rates and charges, and that the utility bears the burden to substantiate its projections. Therefore, the ALJ recommended that the Commission adopt the 2017 calendar year as the projected test year.

ABATE excepts, reiterating that there is no legal requirement that the Commission adopt a projected test year. Instead, ABATE argues, an historical test year is more desirable because it is a better reflection of future actual expenses than a projected test year.

In reply, Consumers avers that ABATE's claims are unsupported by fact and law, and restates that MCL 460.6a(1) specifically permits a utility to use a projected test year in developing its rates. In addition, Consumers states that in the November 2, 2009 order in Case No. U-15645, the Commission "clearly recognized the necessary distinction between the use of historical and projected test years, and appropriately acted to ensure that it acted pursuant to the newly-enacted Legislative mandate to use a projected test year if requested by the utility." Consumers' replies to exceptions, p. 5. Consumers asserts that because it requested the use of a projected test year in this case, pursuant to MCL 460.6a(1), the company is entitled to use a projected test year to develop its rates, and that ABATE's proposal to use an historical test year should be rejected.

ABATE did not file replies to exceptions.

The Commission agrees with the findings of the ALJ and adopts her recommendation.

IV. RATE BASE

Rate base refers to total utility plant (*i.e.*, the capital invested in all plant in service, plant held for future use, and construction work in progress (CWIP)), less the company's depreciation reserve (consisting of its accumulated depreciation, amortization, and depletion), plus the utility's working capital requirements.

Consumers projected total rate base of $4.402 billion for the test year, which consists of approximately $3.736 billion in adjusted net utility plant, $642.558 million in working capital, and $23.889 million in net unamortized manufactured gas plant (MGP).

Based on the fact that no party took issue, the ALJ recommended that the Commission approve Consumers' requested level of CWIP, and the Commission agrees. PFD, p. 62.

A. Net Utility Plant

1. Gas Transmission and Distribution Capital Expenditures

Consumers requested rate recovery of capital expenditures for gas transmission and distribution of approximately $385 million for 2015, $382 million for 2016, and $540 million for 2017, which, the company stated, is necessary to meet customer reliability, safety requirements, and system deliverability demands. The company maintained that these expenditures will be invested in eight major programs: (1) new business; (2) asset relocation; (3) regulatory compliance; (4) material condition; (5) capacity/deliverability; (6) gas-only service territory automated meter reading (AMR); (7) gas operations other; and (8) gas business services.

The Staff disputed Consumers' test year projections for: (1) pipeline integrity (within the regulatory compliance program); (2) material condition; (3) transmission enhancement for deliverability and integrity (TED-I) (within the capacity/deliverability program); and (4) gas-only service territory AMR. The Attorney General also took issue with the company's method for analyzing capital costs, and disputed Consumers' test year projections for new business, regulatory compliance, capacity/deliverability, and gas AMR programs. Both the Staff and the Attorney General recommended that the Commission reject all contingency expenses that were included in the company's rate base projections.

a. Pipeline Integrity Program

The Staff initially recommended that Consumers' test year capital expenditures for the pipeline integrity program be adjusted from approximately $41.8 million to $23.2 million based on the five-year average of historical spending between 2011 and 2015. However, the Staff revised its recommendation to a projected $27.5 million based on a three-year average of historical spending between 2013 and 2015, which excluded capitalized remediation dig activities of $9.9 million related to Consumers' Line 100A rupture incident in June 2015. The Staff stated that it was persuaded to reduce its adjustment based on the company's "rebuttal arguments and demonstrated expenditures," but "is still concerned by the significant variance of actual expenditures from projected, particularly given the Staff's concerns about certain practices related to capitalization and assessment that impact expenditures under this program." Staff's initial brief, p. 26.

The Staff recommended that the Commission order Consumers to complete further review of its 2015 and 2016 remediation dig summaries and an on-going review of 2017 and beyond, of the company's capitalization of longer-than-50-foot pipe replacements to ensure that Consumers is not inappropriately replacing pipe in longer segments than necessary.

The Staff also requested that the Commission require Consumers to review its pipeline integrity assessment plan (PIAP) for 2015 through 2019. The Staff is concerned that the company may be expending too much time and effort assessing its pipelines more frequently than the federally-mandated seven-year assessment schedule, and instead, could be "directing its efforts toward higher risk pipe." Staff's initial brief, p. 26.

In response to the Staff's concerns, Consumers argued that its projected test year capital expenditures were properly supported with detailed exhibits and testimony. Consumers noted that it is impossible to precisely predict expenses for emergent work. For example, in 2016, the company stated, its actual capital expenditures for the pipeline integrity-transmission program were $13 million more than what was projected. Consumers also contended that its witness provided sufficient testimony in response to the Staff's concern about the number of capitalized remediation digs and the company's remediation practices. And, regarding the Staff's recommended seven-year pipeline assessment schedule, the company asserted that it adheres to a six-year schedule because there is higher risk of unsafe and unreliable pipeline operation and failure to comply with the federal rule if the company maintains a seven-year schedule.

The ALJ acknowledged the importance of Consumers' work related to the pipeline integrity program, but agreed with the Staff that there was a "significant variance between the Company's actual expenditures and those projected," and found "that an adjustment is warranted." PFD, p. 16. However, the ALJ noted that the Staff was aware of Consumers' actual 2016 expenditures for the pipeline integrity-transmission program and that the historical average in the Staff's revised adjustment should have included the 2016 actual expenditures. Therefore, the ALJ found that the historical three-year average of 2014-2016 actual expenditures, excluding the $9.9 million spent on capitalized remediation dig activities in 2015, is $29,559,670, and that

Consumers' projected capital expenditures for the 2017 test year, and for 2018 and 2019, should be reduced to this amount.

In response to the Staff's request that Consumers be directed to review its pipeline remediation practices and its PIAP for 2015 through 2019, the ALJ found that the company's witness adequately addressed the Staff's concerns in rebuttal testimony, and therefore, she rejected the Staff's recommendation.

Consumers excepts to the ALJ's recommended $9.9 million adjustment for remediation dig activities. Consumers asserts that "neither Staff nor the ALJ provided an explanation or analysis of why those remediation costs should be excluded from the cost data Staff used for calculating costs to be included in rate base." Consumers' exceptions, p. 4. As a result, the company states, the ALJ's recommendation should be rejected.

In exceptions, the Staff asserts that Consumers' witness failed to explain why the company is using longer pipe segments than are required for remediation, and assessing lower-risk pipe ahead of schedule. In response to the company's contention that it replaces pipe "more frequently than required because it is difficult to schedule its replacement," the Staff states that "the benefit of such early replacement versus the cost to the ratepayer should be assessed, to make sure that replacement expenditures are used wisely." Staff's exceptions, p. 3.

In reply, Consumers argues that the company "reviews each project individually to determine the length of pipe needed to ensure the safe operation of the pipe and adequate spacing for pipe replacement." Consumers' replies to exceptions, p. 10. The company states that although joints of pipe are usually 40-42 feet in length, Consumers adds five feet of length on each side of the existing girth welds to minimize the impact of the heat-affected zones of the existing welds. 7 Tr 1164. Consumers contends that the added length increases the integrity of the pipeline and the new girth welds.

In defense of its use of longer pipe segments, Consumers cites the Staff's admission that, in this case, there is no federal standard that dictates the proper length of pipe segments. Additionally, Consumers states, it must consider "multiple codes and best practices, plus understand each project's variables such as anomaly conditions, tie-in conditions, coating conditions, pipe alignment, and site conditions." Consumers' replies to exceptions, p. 11. The company also reiterates that it uses both the seven-year federally-mandated inspection cycle and a six-year assessment schedule in order to ensure that it can remain in compliance with the federal rule.

In reply to Consumers, the Staff states that on page 23 of its initial brief, it discussed the $9.9 million related to Consumers' 100A incident, and referenced Exhibit S-10.10. Staff's replies to exceptions, p. 2. The Staff notes that Exhibit S-10.10 details Consumers' costs for the unexpected rupture of Line 100A. Because the rupture occurred in 2015 and was unanticipated, the Staff argues that the costs for the rupture are not expected to recur in the upcoming test year. Therefore, the Staff asserts, the $9.9 million expense for Consumers' 100A incident should not be considered in the average for test year expenses and beyond.

Like the Staff and the ALJ, the Commission finds that there is a considerable variance between Consumers' actual and projected expenditures for the pipeline integrity program and that an adjustment is necessary. However, the Commission agrees with the ALJ that the company's actual 2016 expenditures should have been included in the Staff's revised adjustment. In addition, the Commission finds persuasive the Staff's analysis, and the ALJ's recommendation, to adopt the Staff's proposed $9.9 million adjustment for Consumers' Line

100A incident in June 2015. Therefore, the Commission adopts the ALJ's calculation of the historical three-year average of 2014-2016 actual expenditures, excluding the $9.9 million spent on capitalized remediation dig activities in 2015, for a projected capital expenditure for the 2017 test year, 2018, and 2019, of $29,559,670.

The Commission is cognizant of the Staff's concerns regarding Consumers' PIAP for 2015 through 2019, and the benefit/cost to ratepayers for early assessment and remediation of pipe and the use of longer-than-standard pipe segments. The Commission supports the company's efforts to continue to assess its pipeline in compliance with federal rules and to keep its pipeline safe and operational. However, the Commission expects that in future rate case filings, Consumers shall provide detailed and sufficient evidence to demonstrate that pipeline assessment and replacement expenditures are being used prudently.

b. Material Condition Program

The material condition program addresses leaks and deterioration issues that affect system integrity, reliability, and safety, and is comprised of the following subprograms: (1) enhanced infrastructure replacement program (EIRP)-distribution; (2) EIRP-transmission and storage; (3) material condition non-modeled; and (4) material condition renewals.

The Staff did not dispute Consumers' projected 2017 capital expenditures of approximately $67.7 million for the EIRP-distribution and EIRP-transmission and storage. The Staff stated that, as in Case No. U-17882, it "continues to generally support the inclusion of vintage service lines materials as part of EIRP main replacement projects as well as service line only projects as part of the EIRP," and that the Commission should require Consumers:

> to develop and include reporting elements for the service line only replacement projects for both EIRP planning and performance reports and that the Company should also include in the planning report a leak rate analysis, including corrosion leak rate and overall leak rate analysis, for services lines by material type. Staff

> further recommends that in the performance report the Company should include a report of the service line only projects that includes the total number of vintage service lines replaced by vintage service line material type.

7 Tr 1786.

The Staff supported Consumers' definition and projected expenditures for the material condition renewals program. However, based on a five-year average from 2011-2015, the Staff recommended that Consumers' 2016 and 2017 projected expenditures for the material condition non-modeled program be reduced from $33.879 million and $44.993 million, respectively, to $17.4 million annually for each program. The Staff explained that Consumers "failed to identify the number of service line replacements or repairs projected to substantiate the significant increase." Staff's initial brief, p. 21. The Staff also disputed the company's inclusion of vintage service line replacements that are within the proposed scope of the EIRP in the material condition non-modeled program. Finally, the Staff requested that the Commission require Consumers to amend its reporting requirements for non-EIRP programs in Exhibit A-28 to include the reporting requirements set forth in the Staff's testimony. *See*, 7 Tr 1793-1794.

Consumers responded that it provided adequate testimony and exhibits explaining that "the increase in expenditures associated with the Material Condition Non-Modeled Program is due to the Company's efforts to reduce scheduled actionable leaks through full service replacement and the replacement of vintage material services." Consumers' initial brief, p. 13. Consumers asserted that it has experienced an increased number of system leaks due to an aging and deteriorating system, and frost from two consecutive severe winters, and that its proposed expenditures are necessary to address these issues. Therefore, the company requested that the Commission reject the Staff's proposed adjustments.

Consumers agreed to provide the additional information requested by the Staff to the extent the information is readily available and can be reasonably obtained. Consumers' initial brief, pp. 12, 20. The company requested to meet with the Staff to more clearly define the information sought.

The ALJ agreed with the Staff that Consumers failed to provide specific evidence identifying the number or cost of the proposed service line replacements or repairs, and therefore, "leaves this PFD without the ability to determine whether the Company's proposed expenditures are reasonable and prudent." PFD, p. 20. As a result, the ALJ recommended that the Commission adopt the Staff's proposed adjustment and reduce Consumers' 2016 and 2017 material condition non-modeled program expenditures to $17,400,000 each year. The ALJ also recommended that the Commission require Consumers to collaborate with the Staff to develop and implement the additional reporting requirements for non-EIRPs requested by the Staff.

In exceptions, Consumers disagrees with the ALJ's use of a five-year average to develop the projected costs, noting that MCL 460.6a(1) permits a utility to base its rates on a forward-looking projected test year. According to Consumers, the use of projected costs is "especially reasonable" for the material condition non-modeled program because the program addresses emergent issues regarding regulatory compliance and employee safety, and the five-year historical average does not account for the "growing nature of this work." Consumers' exceptions, p. 6.

In addition, Consumers disputes the ALJ's determination that the company failed to provide adequate evidence regarding the number and cost of the service line replacements or repairs. The company reiterates that it is impossible to "specify with 100% certainty the exact level of costs to be incurred or lines to be repaired or replaced" regarding the emergent work in the program. Consumers' exceptions, pp. 6-7. However, Consumers argues, the projected costs are necessary to properly and safely maintain the system.

Consumers notes that the ALJ appears to have agreed with the Staff that it is inappropriate to include vintage service line replacements in the proposed scope of the EIRP and the material condition non-modeled program. The company states that it has not yet received Commission approval to include the costs of vintage service line replacement in the EIRP, and as a result, included the costs in the projection for the material condition non-modeled program for the test year and the investment recovery mechanism (IRM) periods. In the event the Commission finds that vintage service line replacement costs should be included in the EIRP, rather than the material condition non-modeled program, Consumers asserts that the annual EIRP costs should be increased from $75 million to $90 million. In addition, the company requests that the test year and IRM annual expenses for the material condition non-modeled program costs should not be reduced until the vintage service line replacement costs are included in the EIRP costs, and the EIRP annual cost is correspondingly increased from $75 million to $90 million. Consumers' exceptions, p. 8.

Regarding the ALJ's recommendation for additional reporting requirements for the non-EIRP programs, Consumers states that it intends to fully cooperate with the Staff. The company agrees that the reporting requirements listed on Exhibit A-28 for EIRP and non-EIRP programs should be adopted, and it will continue to work with the Staff to develop additional reporting metrics. Although Consumers asserts that the Staff is requesting information that is unclear and unavailable regarding leak mitigation, company-initiated work, service line retirement, and leak rate analysis, the company states that it will provide currently-available information and will consult with the Staff to provide additional information once the definition of data points is clarified.

The Staff replies that although utilities are permitted to project future costs, they are still required to specify and quantify those costs. Staff's replies to exceptions, p. 4. Consumers claims that it cannot separate the information regarding the leak mitigation program and company-initiated work, however the Staff states that the company's response "identifies a fault in the reporting system that can and should be corrected by the Company." *Id.*, p. 5.

The Commission finds persuasive the ALJ's determination that Consumers failed to provide specific and adequate evidence identifying the number or cost of the proposed service line replacements or repairs for the material condition non-modeled program. Consumers claims that it is impossible to predict with certainty the costs for emergent work. Accordingly, the Commission finds that the five-year average adopted by the ALJ provides a reasonable and prudent estimate of projected emergent work for the program. Therefore, the Commission adopts the ALJ's adjustment and reduces Consumers' 2016 and 2017 material condition non-modeled program expenditures to $17,400,000 each year.

The Commission also adopts the findings and recommendation of the ALJ regarding Consumers' proposed increase to the annual EIRP expense. The Commission finds that the company did not sufficiently demonstrate projections for future work that would justify the proposed increase. In the event the company desires to increase annual EIRP expense, in its next rate case filing, Consumers shall specifically define and quantify the projected amount of work justifying the increase.

In addition, the Commission adopts the ALJ's recommendation that Consumers and the Staff collaborate to develop and implement the Staff's additional reporting requirements for the EIRP and the non-EIRP.

c. Transmission Enhancement for Deliverability and Integrity Program

Consumers projected capital expenditures of $15.709 million for 2015, $22.620 million for 2016, and $120.682 million for 2017, 2018, and 2019, for its TED-I program.

The Staff did not dispute Consumers' TED-I-related expenditures for 2015, but recommended a $15.6 million reduction and a $48.1 million reduction to the company's 2016 and 2017 projected expenditures, respectively, for a total disallowance of $63.719 million, of which $27.4 million is identified by the Staff as non-contingency related. Regarding the $27.4 million non-contingency adjustment, the Staff explained that after an audit request and two discovery requests by the Staff and the Attorney General for 2016 year-end projected capital expenditures on a project-level basis, Consumers failed to provide the requested information. 7 Tr 1804. Therefore, the Staff asserted, Consumers' rate recovery should be limited to its 2016 actual expenses that were provided in response to Staff Audit Request #118.

In addition, the Staff contended that Consumers failed to provide sufficient justification for the capital expenditures for 22 projects to install pressure-limiting devices (PLDs) between 2016 and 2021. The Staff noted that at least one of the projects identified for rate recovery had a probable violation of 49 CFR 192.195 of the Commission's Gas Safety Standards, R 460.20101 *et al.*, in June 2016, and that the company acknowledged that "further information is necessary to conclusively determine if any of the remaining projects identified are not currently in compliance with the requirements of 49 CFR 192.195." 7 Tr 1801. The Staff asserted that Consumers should not be permitted to fully recover capital expenditures for projects that fail to comply with federal standards due to Consumers' failure to install required overpressure protection.

Consumers responded that it provided adequate evidence justifying the projected TED-I capital expenditures, citing its witness' testimony in support. The company also argued that the PLD expenses are necessary for Consumers to remain in compliance with 49 CFR 192.619 and 49 CFR 192.195 of the Commission's Gas Safety Standards, R 460.20101 *et al*.

The ALJ agreed with the Staff and found that Consumers failed to provide specific and adequate evidence to support the 2016 TED-I capital expenditures on a project-level basis. The ALJ stated that, "The Company's response, via Ms. Bowers' rebuttal testimony, that the proposed PLD installation locations come from a combination of Parts 49 CFR 192.619 and 49 CFR 192.195 of the Gas Safety Code, remains insufficient as it still fails to justify why the cost of the installation of the devices should be borne by the ratepayer." PFD, p. 23. Therefore, the ALJ recommended that the Commission adopt Consumers' 2016 actual expenditures of $7,033,000.

Regarding the Staff's concerns about the capital expenditures for the 22 projects to install PLDs between 2016 and 2021, the ALJ noted that in response to Staff Audit Request #118, Consumers identified TED-I projects for 2015-2023, and provided a project description, year, and current cost estimate. However, the ALJ found that the company failed to provide a "breakdown of the material, labor, contractor, engineering, and contingency costs" or a timeline for each project. PFD, p. 24. In addition, the ALJ stated, Consumers' testimony and initial brief notably do not address the Staff's determination of a probable Part 49 CFR 192.195 violation at one of the project sites. As a result, the ALJ recommended that the Commission should adopt the Staff's proposed $27,444,000 non-contingency-related disallowance for TED-I capital expenditures.

In exceptions, Consumers argues that Exhibit A-24 provides TED-I project expenditure amounts for 2015-2017. The company asserts that, while Exhibit S-10.13 provides a detailed explanation of the projects, the attachments provide the "project description, year and current cost estimates, and the type of pipe to be replaced and proposed pipe to be installed." Consumers' exceptions, p. 10. In addition, the company states, Exhibit S-10.13 also provides detail regarding PLD installation.

In response to the ALJ's determination that the company failed to justify that ratepayers should be responsible for the expense of PLD installation, Consumers argues that federal law requires it to install the PLDs. Consumers states that, in the past, it could comply with federal requirements by relying on pressure drop on the system and the use of remotely-operated valves. However, the company claims that the installation of PLDs removes the element of human error associated with its previous method of compliance. Responding to the Staff's contention that the company should have incurred the cost of installing PLDs at the time of construction or connection to other pipelines, Consumers maintains that its "previous manner of achieving regulatory compliance for overpressure protection was considered satisfactory" by the Staff. Consumers' replies to exceptions, p. 12. Therefore, Consumers asserts, it was not reasonable for the company to incur the cost of PLD installation at the time of construction or pipeline connection.

In reply, the Staff states that it "identified specific situations where, from a regulatory compliance perspective, the PLD should have been installed decades before the present day." Staff's replies to exceptions, p. 6. The Staff notes, for example, that a PLD should have been installed on Line 8100 Summerton Road Valve Site at the time of construction in the late 1980s or when the operating pressures of the connecting pipelines required the installation of overpressure protection.

The Commission adopts the ALJ's recommendation to reduce Consumers' 2016 projected TED-I expenditures to $7,033,000. The Commission finds that Consumers failed to provide specific evidence to support the TED-I capital expenditures on a project-level basis and failed to explain why the cost of the installation of the devices should be borne by ratepayers. In addition, the Commission finds that the company did not specifically identify the expenses for material, labor, contractor, engineering, contingency costs, or a timeline for each PLD installation project, and therefore, adopts the ALJ's recommended $27,444,000 non-contingency-related disallowance.

d. Gas Only Service Territory Automated Meter Reading Costs

Consumers projected gas-only service territory AMR capital expenditures of approximately $4.5 million for 2016, and $22.3 million for 2017.

The Staff recommended that the Commission disallow approximately $1.3 million for 2016 and $4.6 million for 2017 for software and systems development, and approximately $3.5 million for 2017 for modules, due to Consumers' failure to provide sufficient support for the expenses. In addition, the Staff requested a disallowance of $3.956 million for AMR contingency expenditures.

The Attorney General requested that the Commission reject a total of $23.324 million of AMR capital expenditures for 2014-2017, and should continue to reject future expenses until Consumers is able to demonstrate that the risks of the AMR program are shared equitably. He argued that the company's financial business case is deficient and its benefit/cost analysis is "overly optimistic and unrealistic." 7 Tr 1300-1301.

Consumers responded that it properly supported the requested expenditures through its responses to Staff Audit Request #154 in Case No. U-17882, and Staff Audit Requests #103 and #200 in this case. Consumers asserted that these responses provide information about the modules that will be used for the gas AMR program, the number of modules to be purchased and installed for each year of the program, and details regarding the costs for its proposed software and system development activities. Consumers' initial brief, p. 16.

In addition, Consumers averred that the Attorney General is suggesting an alternative cash flow approach to determine the net present value (NPV) of the project. However, the company stated that the Attorney General's "suggested methodology has previously been rejected by the Commission in Case Nos. U-17087 and U-15645 (Remand) in its analysis of NPV methods for the Company's Advanced Metering Infrastructure . . . Program." Consumers' initial brief, p. 27.

The ALJ found that Consumers thoroughly supported all but one of its projected expenditures for the AMR program. The ALJ noted that "in Case No. U-17087, the Commission considered and rejected the Attorney General's same criticism of the utility's NPV methodology raised in the context of the Company's AMI program and ultimately concluded that the Attorney General's proposed reduction to the forecasted benefits was 'arbitrary and unsupported.'" PFD, p. 40, citing the June 28, 2013 order in Case No. U-17087, pp. 3, 8-9. In addition, the ALJ stated that Consumers provided evidence demonstrating that its 2016 actual capital expenditures exceeded the projected amounts by $44.418 million. Therefore, the ALJ recommended that the Attorney General's proposed reduction should be rejected.

However, the ALJ agreed with the Staff and found that Consumers failed to provide adequate support for its proposed expenditures for modules and software and systems development. After a review of Consumers' responses to Staff Audit Requests #103, #109, and #110, the ALJ noted that:

> the Company's position that the needed work effort for installation and integration of the software collection systems "will be an outcome of detailed design workshop, at which time detailed costs will be determined," and that details of the planned installation schedule for the modules "will be finalized during the first quarter of 2017" is insufficient for this PFD to make a determination whether such expenditures are reasonable and prudent.

PFD, p. 27, citing Exhibit S-15.4, pp. 1-3. As a result, the ALJ recommended that the Commission adopt the Staff's proposed disallowance.

In exceptions, Consumers cites its witness' testimony explaining that the AMR program is for customers who are not a part of the Smart Energy Program, and that there are multiple financial benefits to customers such as significantly reduced meter reading expense, improved billing accuracy, a reduced number of re-reads and re-billings, a reduced rate in energy theft, and increased employee safety. In addition, Consumers reiterates that it provided the Staff with exhibits demonstrating the data for the modules, the company's business case, the module numbers and cost per module, and information about the software and systems development. Regarding the expense for the program, Consumers states, "As with the use of a projected test year, the Company's expenditure levels are forward looking. Thus, but its very nature, the actual expenditures necessary are unknown. The Company maintains that it did support its projections." Consumers' exceptions, p. 15.

The Attorney General did not file exceptions.

The Commission agrees with the ALJ. Although the company provided some explanation regarding the data and the benefits of the AMR program, Consumers failed to set forth specific expenses for the modules and the software and systems development. As noted by the ALJ, Consumers admitted that in regards to the software system, "detailed costs will be determined" at a future workshop, and that the details for the installation of the modules "will be finalized during the first quarter of 2017." Exhibit S-15.4, pp. 1-3. The company also admitted in its exceptions that actual necessary expenses are unknown. Thus, without specific expense information for modules and software and systems development, the Commission cannot determine whether the company's projected expenses for these items are reasonable and prudent, and therefore adopts the ALJ's recommended disallowance.

e. New Business

Regarding the installation of main services and meter stands, large new business projects, the Customer Attachment Program (CAP), and new business meters, Consumers projected approximately $73.4 million in capital expenditures for 2016, and $82.5 million for 2017.

The Attorney General recommended reductions of approximately $5 million for 2016, and $14.2 million for 2017. The Attorney General explained that these disallowances are warranted because "The year-to-date September 2016 information, when compared to the capital expenditures for the same 9-month period in 2015, shows that actual capital expenditures in 2016 are running significantly below 2015 by $5,055,000." 7 Tr 1293. Using the same method, the Attorney General concluded that the 2017 capital expenditures "are likely overstated by $14.2 million." *Id.*, p. 1295.

Consumers disputed the Attorney General's method for determining his proposed reductions. According to the company, the Attorney General selectively chose to emphasize the subset, "new business," in his comparison of September 2016 year-to-date expenditures and 2015 actual expenditures, and failed to include the programs in which Consumers exceeded 2015 expenditures and projections. Consumers asserted that if its projected expenditures are reviewed as a whole, and not selectively, as done by the Attorney General, the company exceeded the

2015 actual amounts in each of the major capital programs, except new business, and exceeded the September 2015 amount by over $59 million.

The ALJ agreed with Consumers that the Attorney General's proposed disallowances should be rejected. The ALJ stated that the Attorney General's analysis:

> was incomplete inasmuch as his comparison of the September 2016 year-to-date expenditures with the Company's actual 2015 expenditures overlooked 4 of the 5 programs that exceeded actual amounts (by $54.3 million) and focused solely on the 1 program (New Business) wherein the 2016 projected amount fell short of the 2015 actual amount (by $5,055,000).

PFD, p. 34. In addition, the ALJ found that Consumers' testimony sufficiently supported the company's proposed new business expenditures.

In exceptions, the Attorney General argues that his witness performed a complete analysis of the capital expenditures and that he did, in fact, note that there were some programs that were exceeding costs. However, the Attorney General states, after considering the higher expenditures in these other programs, he concluded that it was appropriate to focus on programs where Consumers is not likely to spend the projected amount so that ratepayers are not overcharged.

In reply, Consumers continues to support adoption of its proposed new business expenditures based on the positions set forth in its testimony and briefs.

The Commission agrees with the findings and recommendation of the ALJ. As noted by the ALJ, the Commission finds that the Attorney General's analysis improperly focused on the new business program, and overlooked other programs in which Consumers exceeded prior-year expenditures and projections. When examined as a whole, Consumers' projected 2016 and 2017 capital expenditures for the installation of main services and meter stands, large new business projects, CAP, and new business meters are reasonable and prudent, and the Commission finds that the Attorney General's proposed disallowances should be rejected.

f. Regulatory Compliance

For the regulatory compliance program, Consumers projected approximately $40.3 million in capital expenditures for 2016, and $64.7 million for 2017. The Attorney General argued that Consumers' response to Staff Audit Request #70 failed to explain $11.8 million of the company's proposed expenditures for the pipeline integrity program for transmission lines. As a result, the Attorney General recommended a $5.6 million disallowance that would align Consumers' proposed 2017 expenditures with 2015 actual expenditures. In response, Consumers cited 54 pages of audit and discovery responses in Exhibit S-10.10 that the company claims provide support and explanation for the program.

The ALJ referenced her decision in the pipeline integrity-transmission section, noting that she found that Consumers sufficiently established that its proposed expenditures are reasonable. The ALJ stated that:

> except to surmise that "the Company has not yet formulated concrete plans to spend the remaining $11.8 million," the Attorney General has proffered no substantive argument for his proposed reduction and no acknowledgment of the fact that the Company's year-to-date September 2016 expenditures of $33,823,000 in the Pipeline Integrity-Transmission have exceeded the Company's projected total amount of $19,130,000 by $14,693,000.

PFD, p. 36, citing the Attorney General's initial brief, p. 54. Therefore, the ALJ recommended that the Commission reject the Attorney General's proposed disallowance.

Although the ALJ accepted Consumers' explanation justifying the $11.8 million, in exceptions, the Attorney General argues that her determination misses the mark. He notes that the company described some of the costs as primarily "emergent," which means that the costs are usually unknown until they occur. The Attorney General states that "Similar to contingencies, these emergent costs appear to cover the unknowns and what-ifs, and likewise should not be included in rate base." Attorney General's exceptions, p. 10.

In reply, Consumers states that the amounts shown in the response to Staff Audit Request #70, which is included in Exhibit S-10.10, did not include capital loadings or emergent remediation expenditures, and these items account for the amounts that the Attorney General argued were not in Exhibit S-10.10. Consumers' replies to exceptions, p. 17. Consumers asserts that Exhibit S-10.11 shows that as of September 2016, the company had spent approximately $14.7 million more than projected in the pipeline integrity-transmission program. Consumers states, "That increase in costs demonstrates the validity of including emergent costs that arise in the course of a year in that program and supports the Company's requested recovery." *Id.*, p. 18.

The Commission agrees with the ALJ that, regarding the pipeline integrity-transmission program, Consumers sufficiently demonstrated in its audit and discovery responses that the company's proposed expenditures are reasonable. The Commission finds that the Attorney General's analysis was insufficient to rebut the company's evidence that its 2016 actual costs were $14.7 million more than projected. Therefore, the Commission adopts the ALJ's recommendation to reject the Attorney General's proposed disallowance.

g. Capacity/Deliverability Program

For its capacity/deliverability program, Consumers projected $79.1 million for 2016, and $180.4 million for 2017. The Attorney General recommended a $2 million reduction to Consumers' proposed expenses for its TED-I projects. And, because the Commission has yet to approve the company's September 2016 application pursuant to 1929 Act 9, MCL 483.101 *et seq*. (Act 9) in Case No. U-18166, he requested that the projected 2017 expense of $116.2 million for the Saginaw Trail Pipeline be rejected.

Consumers contended that the Attorney General used a faulty methodology and failed to consider recent information showing that not only did the company exceed the projected amount for the TED-I program, but also exceeded the 2015 year-to-date September amount by $59 million. Consumers' initial brief, p. 25. Regarding the Saginaw Trail Pipeline expenses, Consumers explained that "The remaining expenditures were for final restoration of projects already completed and material procurement for the Line 2800 (Saginaw Trail Pipeline) project." *Id.* In addition, Consumers states that it submitted a settlement agreement on March 9, 2017, in Case No. U-18166, recommending that the Commission issue an order granting Consumers an Act 9 certificate of public convenience and necessity to construct the Saginaw Trail Pipeline.

The ALJ found that the Attorney General's recommended disallowances should be rejected. Once again, the ALJ stated that he failed to recognize that Consumers' actual expenditures through September 2016 have already exceeded the projected test year amount. In addition, regarding the $116.2 million expense for the Saginaw Trail Pipeline, the ALJ noted that the Commission approved a settlement agreement on March 28, 2017, in Case No. U-18166, which renders the Attorney General's argument moot.

No exceptions were filed, and the Commission adopts the findings and recommendations of the ALJ.

2. Gas Compression and Storage Capital Expenditures

Consumers requested rate recovery of gas compression and storage (GCS) capital expenditures of $98.369 million for 2015, $102.218 million for 2016, and $119.115 million for 2017.

The Staff argued that Consumers failed to provide consistent and adequate support for the capital expenditures associated with the St. Clair Upgrade and the Freedom Upgrade projects, and the company's projected 2017 compression and storage fields (CSF) expense of $48.822 million. The Staff recommended that the St. Clair Upgrade project expenses be reduced by approximately $1.07 million for 2016 contingency costs, and $15.810 million for 2017 non-contingency capital expenditures. Regarding the Freedom Upgrade project, the Staff recommended reductions of $1.885 million for contingency costs, and $3.687 million for 2017 non-contingency capital expenditures. However, the Staff withdrew its recommended reduction to the CSF expense, provided Consumers adopts certain reporting requirements:

> The Company should file in this docket a performance report by April 30 of each year that details the prior calendar year's performance. The report filed should be consistent with the information as provided in Company Exhibit A-94 and Workpaper DBK-6, which is included on the record in Staff Exhibit S-10.9 (including all capital expenditures for gas storage and compression, and should specifically identify any line items that are included in the Gas Well Rehabilitation Project Plan (Exhibit A-95)). The report should discuss any significant findings or rehabilitation required in the project and should include updated projections for well logging plans and associated capital expenditures for the remainder of the capital program.

Staff's initial brief, p. 14.

The Attorney General proposed that Consumers' projected GCS 2016 capital expenditures be reduced by $3.849 million for 2016, and $20.746 million for 2017, in order to align the capital expenditures with 2015 amounts, less the contingency amounts. He asserted that the reductions are necessary because the company failed to timely provide him with the actual year-to-date September 2016 capital expenditures so that he could perform a reasonable analysis.

Consumers agreed that there was an inconsistency between an exhibit and an audit response provided to the Staff, and corrected the amount assigned to the construction packages portion of the St. Clair Upgrade project for 2017. According to Consumers, the adjustment increased the 2017 projected expenditures for the St. Clair Upgrade project to $33.672 million, and the project total to $181 million, which "is within the Board approved amount – as the Board approved amount allows for a 10% variance." 6 Tr 979. Regarding the Freedom Upgrade project, Consumers explained that the inconsistency identified by the Staff is due to the company's acceleration of $3.7 million in 2017 funds to cover the remaining construction expenses required to ensure the temporary compressors were in service by January 2017 and to provide additional time for Phase 2 engineering, which, according to the company, will reduce overall project expenses. *Id.*, p. 980.

In response to the Attorney General, Consumers disputed that it failed to timely provide the requested information. The company contends that it initially provided the information via a discovery response more than a month before testimony was due. However, according to Consumers, the Attorney General informally requested a voluminous supplement to the discovery response only four business days before testimony was due. Consumers stated that it complied with his request, but was only able to provide the information one business day before the deadline.

The ALJ agreed with the Staff that Consumers' projected 2017 expense of $48.822 million for CFS is reasonable and prudent, should be adopted, and should be accompanied by the Staff's recommended reporting requirements. However, the ALJ rejected the Staff's proposed non-contingency adjustments to the St. Clair Upgrade and the Freedom Upgrade projects. She determined that Consumers sufficiently explained the inconsistencies identified by the Staff, and that the company's projected amounts for the St. Clair Upgrade and Freedom Upgrade projects are reasonable and prudent, and should be approved.

Regarding the Attorney General's claim that he failed to timely receive actual, year-to-date, September 2016 capital expenditures, the ALJ determined that based on Consumers' explanation of the incident and the fact "that the Attorney General neither acknowledges nor disagrees with this testimony in his Initial Brief, this PFD finds it cannot be said that Mr. Coppola lacked the requested information necessary for his analysis prior to the December 22, 2016 filing date of his direct testimony." PFD, p. 47. Therefore, because this was the only basis for the Attorney General's proposed reductions, the ALJ found that his recommendation should be denied.

On page 3 of its exceptions, the Staff argues that "Although . . . the Company filed amended audit responses to Staff Audit Request #114 in rebuttal Exhibit A-96 . . . to state that the board allowed a 10% variance on the approved $165 million St. Clair Upgrade project up to $181 million, Staff continues to recommend allowance of the board approved amount of $165 million." The Staff explains that the project is not complete and the Staff and the Commission have yet to review final expenditures, and therefore, the 10% variance is akin to a contingent expenditure.

In reply, Consumers states that its witness provided testimony that the board of director's approved budget was actually $181 million, *i.e.*, $165 million for the project, plus an approved 10% variance. The company disputes that the 10% variance is a contingency, and argues that the Staff failed to support its position.

The Commission agrees with the ALJ and approves Consumers' projected 2017 expense of $48.822 million for CFS, accompanied by the Staff's recommended reporting requirements. The Commission adopts the board-approved amount of $165 million for the St. Clair Upgrade and Freedom Upgrade projects, but rejects the 10% variance. As the Commission discusses below, contingency amounts are amounts set aside for cost items whose occurrence is uncertain, and inclusion of such items in rate base is not sound ratemaking practice. The Commission finds that the 10% variance is akin to contingency and, therefore, should be rejected.

3. Business Technology Services Capital Expenditures

For capital expenditures related to information technology (IT), Consumers projected $42.866 million for 2015, $32.880 million for 2016, and $27.694 million for 2017. The company stated that Exhibit A-67 sets forth "the gas allocation of projected capital expenditures to procure, install, and implement the software and infrastructure . . . to meet business requirements." 4 Tr 196. According to Consumers, some of the capital investments made in IT projects during 2014-2015 involve: (1) significant improvements to customers' digital experience; (2) replacing hardware that has reached the end of its useful life; and (3) projects to ensure that the company's information systems are protected from cyber threats. *Id.*, p. 201.

The Staff recommended disallowances to Consumers' projected 2015-2017 IT expenditures based upon inadequate and inconsistent information provided by the company. The Staff acknowledged that in its rebuttal testimony, Consumers provided adjusted project allocation percentages for the categories of network, new computers, and software intangible. However, the Staff argued that the company's updated analysis varied from its audit response, and the changes were not sufficiently supported. Therefore, the Staff recommended revised disallowances of $1.2 million for 2015, $8.839 million for 2016, and $2.583 million for 2017. The Staff explained that the revised disallowances were calculated using the total gas and electric project expenditures identified in Consumers' audit response, and after applying the new allocations, the gas portion of the project costs was determined.

The Attorney General supported Consumers' IT capital expenditures for the Web Foundation, CE Website Redesign, and Web Content Management, but recommended a $9.9 million reduction for three Digital Customer Experience projects in 2015-2017. The Attorney General argued that Consumers failed to justify the need and the economic necessity for these projects, and that the company designed a more detailed and sizable product than necessary.

In response to the Staff, Consumers contended that it provided sufficient testimony to support the company's IT capital expenditures. The company stated that "To include detailed explanations . . . for over 140 unique project line items would have been both unwieldy and unnecessary." 4 Tr 222. Consumers argued that the Staff's proposed adjustments should be rejected because the Staff's witness made invalid assumptions, the company inadvertently omitted expenses, and the Staff wrongly assumed that the proposed 2017 project costs are equivalent to the costs included in the business case. In addition, Consumers is perplexed that the Staff supported the company's IT capital expense in Consumers' last rate case, Case No. U-17990, but found the evidence inadequate in this case, even though the company's evidentiary presentation is consistent with Case No. U-17990.

Consumers recommended that the Commission adopt its projected IT capital expenditures as set forth in Exhibit A-112. However, in the event the Commission adopts the Staff's proposed disallowances, Consumers requested that the Commission include the company's proposed $7.724 million for 2016 Gas Code Compliance costs because the Gas Code Compliance Program was a budget transfer to Consumers' IT Department and the program costs were inadvertently excluded from the 2016 project list supplied to the Staff.

Responding to the Attorney General, Consumers disputed that the IT capital expenditures are unnecessary. The company cited testimony and exhibits detailing the significant customer benefits and participation rates in the projects, and stating that "a 2016 Company survey of its customers revealed that 83.2% of its website users were able to accomplish their goal while using the website, compared to just 41.5% in the 2015 survey." 4 Tr 231.

The ALJ adopted the Staff's revised adjustments, finding that the disallowances are reasonable and prudent. Although she acknowledged that Consumers attempted to address the Staff's concerns in its rebuttal testimony, the ALJ determined that the company "failed to adequately explain the initial omissions in the Company's response to Staff's Audit Request #101 or the basis for the newly identified projects to which a zero cost has been attributed." PFD, p. 53. Therefore, the ALJ found that Consumers' projected IT capital expenditures should be reduced by $1.2 million for 2015, $8.839 million for 2016, and $2.583 million for 2017. However, the ALJ found persuasive Consumers' explanation for its inadvertent omission of the proposed $7.724 million for 2016 Gas Code Compliance costs, and recommended approval of this expense.

Regarding the Attorney General's proposed disallowances, the ALJ found that Consumers provided sufficient evidence to justify the capital expenditures for the 2-Way Customer Communication, DCE Website Replacement R2, and DCE Website Replacement R3. The ALJ determined that the Attorney General failed to present a persuasive analysis or discussion of his recommended disallowance.

In exceptions, Consumers maintains that its 2017 test year IT capital expenditures should be adopted based on the positions set forth in its testimony and briefing.

The Staff excepts, stating that the ALJ incorrectly offset disallowance of gas transmission and distribution capital expenditures with $7.724 million for Gas Code Compliance costs. The Staff argues that the "$7.724 million was an expense already recorded in IT, and incorrectly double recorded in the Gas Code Compliance Program. Thus, it should be merely disallowed." Staff's replies to exceptions, p. 5.

In replies to exceptions, Consumers disputes that the ALJ double-counted the $7.724 million. Instead, Consumers argues that the ALJ found that the company sufficiently explained why the expenditure was excluded from the response to Staff Audit Request #101.

The Commission adopts the findings and recommendations of the ALJ. Although Consumers claimed that it was unmanageable to include detailed descriptions for over 140 unique project line items, the Commission agrees with the ALJ that the company failed to provide sufficient evidence to support the total amount projected for IT capital expenditures. The Commission also agrees with the ALJ's determination that the Attorney General failed to properly support his proposed disallowance. Therefore, the Commission adopts the ALJ's recommendation to approve the Staff's revised reductions of $1.2 million for 2015, $8.839 million for 2016, and $2.583 million for 2017. In addition, the Commission adopts the ALJ's finding that Consumers inadvertently omitted $7.724 million for 2016 Gas Code Compliance costs, and approves this expense.

4. Gas Advanced Metering Infrastructure

Consumers stated that it began installing gas advanced metering infrastructure (AMI) meter modules in 2015, and expects to complete installation by the end of the 2017 test year period. According to the company, smart meters and modules comprise approximately $750 million in capital expenditures for 2007-2017, $90.101 million of which is estimated to be direct and indirect capital costs associated with the gas AMI components. 6 Tr 1048. Regarding the Smart Energy Program, the company projected gas common capital expenditures for 2015-2017 of $55.665 million. Consumers requested that the Commission approve the expenses associated with its AMI investments and determine that its investments satisfy the NPV benefit/cost analysis.

Although the Staff did not recommend adjustments to Consumers' projected AMI capital expense, the Staff requested that the Commission order the company to track its actual test year expenditures. The Staff was concerned about the delay of the project, and recommended that any test year expenditures not spent be deducted from Consumers' projected AMI test year expenditures in its next general rate case. 7 Tr 1812. The Staff also requested that the Commission adopt reporting metrics for the Smart Energy Program, similar to those proposed by the Staff and approved in the January 31 order and the February 28, 2017 order in Case No. U-17990 (February 28 order).

Consumers discounted the Staff's concerns about project delays, asserting that the company has accelerated its installation plan and expects gas AMI capital investments to exceed projected amounts. In addition, Consumers disagreed with the Staff's recommendation that the company track its actual test year expenditures and deduct unspent funds in a future case, arguing that the Staff's request is unreasonable and amounts to a "special reconciliation." Consumers' initial brief, pp. 44-45. However, Consumers supported the Staff's proposed reporting and metrics.

After acknowledging the Staff's concerns about previous project delays and a possible delay to the Smart Energy Program, the ALJ noted that the Staff did not dispute the company's claim that the project is now ahead of schedule. The ALJ found persuasive Consumers' assertion that its gas AMI capital investment will exceed projections, and therefore, recommended that the Commission reject the Staff's proposed tracking of funds or future adjustment. Thus, the ALJ recommended that the Commission approve Consumers' projected AMI capital expenditures of $13.3 million. In addition, the ALJ recommended adoption of the Staff's proposed reporting and metrics, and suggested that the Commission "require the Company to address each of the proposed smart grid metrics in its first report, as Staff requests." PFD, p. 61.

In exceptions, Consumers notes that no party disputed the inclusion of direct and common gas capital expenditures incurred for the gas AMI program for the period of 2007 through 2016, and that the "PFD did not expressly address these historical investments." Consumers' exceptions, p. 25. As a result, Consumers requests that the Commission approve AMI capital expenditures of $76.8 million for 2007-2016.

The Staff excepts, reiterating that any projected test year capital expenditures not spent should be deducted from Consumers' proposed test year expenditures in its next general rate case. The Staff asserts that its recommendation holds the company "accountable to the work they are projecting to complete in the test year. If the company is confident it will *not* be underspending in this program, then this recommendation should be of no concern and have no effect on the next rate case." Staff's exceptions, p. 7 (emphasis in the original).

In reply, Consumers avers that the Staff's recommendation to apply a future projected test year disallowance based on an alleged variance in 2016 spending compared to that projected in Case No. U-17882 "contradicts the black box nature of the Settlement Agreement in that case, to which Staff was a signatory." Consumers' replies to exceptions, p. 21. In addition, pursuant to MCL 460.6a(1), Consumers notes that utilities are entitled to base their rates on a fully-projected test year. The company argues that the Staff's recommendation to disallow AMI capital expenditures in a future rate case amounts to a reverse-looking tracking mechanism that is contrary to MCL 460.6a(1). Consumers states that the Staff is requesting a special reconciliation of gas AMI investments that may occur in a future rate case, which is unreasonable "in light of the Staff's overall support for the program." *Id.*, p. 22.

The Commission agrees with the findings and recommendations of the ALJ, and approves Consumers' projected 2017 AMI capital expenditures of $13.3 million. In addition, the

Commission finds that direct and common gas capital expenditures incurred for Consumers' gas AMI program for the period of 2007 through 2016 of $76.8 million should be approved. The Commission also adopts the Staff's proposed reporting and metrics, and directs the company to address each of the proposed metrics in its first report.

5. Contingency Expenditures

The Staff and the Attorney General recommended disallowance of all contingency costs. The Staff proposed a total disallowance of $47.290 million, which consists of $2.781 million for 2016, and $44.509 million for 2017. The Attorney General recommended a total disallowance of $45.242 million, which is Consumers' forecasted contingency expenditures for 2017. The Staff argued that contingency costs should be excluded because "at this time, [the Staff] cannot make any judgment as to the reasonableness or prudence of these expenditures, as they are based upon uncertainty." 7 Tr 1817. The Staff noted that the company can recover these amounts from ratepayers if and when they are actually spent, after showing that the expenditures were reasonable and prudent. The Staff cited the January 31 order, noting that the Commission denied DTE Electric Company's request to recover contingency costs. The Attorney General agreed with the Staff.

Consumers responded that "use of contingency expenditures is a common and accepted Project Management practice, which is a recognized standard for Project Management professionals." Consumers' initial brief, p. 17. The company asserted that the contingency costs were calculated based on the type of project, the degree of information available, and professional judgment. *Id.*, p. 18. Providing an example, Consumers noted its testimony regarding the company's strategy for projecting contingency costs for the Line 2800 (Saginaw Trail Pipeline) TED-I project. In addition, the company noted that its 2016 preliminary actual capital expenditures for the gas transmission and distribution programs exceeded the projected amount by about $44 million, thus proving that the company's cost projections are conservative. Although Consumers acknowledged that the Commission denied recovery of contingency costs in the company's most recent electric rate case, Case No. U-17990, Consumers nevertheless maintains that contingency costs are not speculative in nature and are not dependent upon the occurrence of an event outside of the utility's control.

The ALJ noted that, in several orders, the Commission has rejected recovery of contingency costs, most recently in the February 28 order. In addition, the ALJ stated that, "while the Company posits that the contingency cost levels sought in this proceeding are 'not speculative in nature, and are not dependent upon occurrences outside the Company's control,' it appears that none of the Company's witnesses were able to provide specific details for any of the projects to which those requested contingency expenditures relate." PFD, pp. 30-31. According to the ALJ, this was further demonstrated by Consumers' response to Staff Audit Request #115, wherein the company acknowledged that the contingency costs associated with the TED-I/Saginaw Pipeline Trail were for unknowns such as weather, underground features not discoverable during the preliminary engineering phase, and any other unexpected environmental issues. Therefore, the ALJ recommended that the Commission reject Consumers' projected contingency expenditures of $47.290 million.

In exceptions, Consumers states that "the contingency amounts included in the Company's projected capital programs are budgeted like any other component of a project budget, are expected to be incurred, and indeed, have historically been incurred as the Company completes its projects." Consumers' exceptions, p. 18. Consumers argues that by withholding the opportunity to recover contingency costs until its next rate case, the Commission is denying the company the right to a fully projected test year permitted under MCL 460.6a. In the event the Commission rejects the company's projected contingency costs, Consumers requests that the Commission provide "guidance on the proofs which would be sufficient to support a decision which allows the recovery of contingency costs included in a utility's projected test year." *Id.*

In replies to exceptions, the Staff and the Attorney General support the ALJ's recommendation for the reasons set forth in their testimony and briefing.

The Commission adopts the findings and recommendations of the ALJ, and notes that the Commission has repeatedly rejected rate recovery of contingency costs. In Case No. U-17735, the Commission determined that "By definition, contingency amounts are amounts set aside for cost items whose occurrence is uncertain. The Commission agrees with the Staff and the ALJ that inclusion of such items in rate base is not sound ratemaking practice." November 19, 2015 order in Case No. U-17735 (November 19 order), p. 11. In Case No. U-17767, the Commission stated that, "while contingency planning is an acceptable budgetary strategy, it is not appropriate for ratemaking . . . . [C]ontingency budgeting is speculative, and shifts all of the risk associated with that item onto ratepayers, allowing for a return of and on an investment that may never be made." December 11, 2015 order in Case No. U-17767, pp. 19-20; *see also, In re Application of Indiana Michigan Power Co,* 307 Mich App 272, 291-293; 859 NW2d 253 (2014). And, in Case No. U-18014, the Commission determined that, "Because Michigan utilities are permitted to rely on fully projected test year costs and revenues, which already introduces a measure of uncertainty in the rate setting process, the Commission finds that it is far too speculative to add contingency amounts on top of that." January 31 order, p. 12. For these same reasons, the Commission finds that including contingency amounts in Consumers' projected capital expenditures is not sound ratemaking practice. Therefore, the company's request for

$47.290 million of contingency costs is denied. As the Commission has previously stated, costs identified as contingency costs in the planning stages of a project may be recovered in a future rate case if they are reasonably and prudently incurred as part of actual expenditures.

6. Accumulated Provision for Depreciation

Consumers' projected 2017 accumulated provision for depreciation is $2,947,973,000. However, the Commission approved new depreciation rates on March 28, 2017, in Case No. U-18127 (March 28 order). As a result, Consumers stated that the depreciation reserve should be decreased by $1.487 million to $2,946,486,000.

The Staff's projected accumulated provision for depreciation is $2,944,182,000, based on the Staff's proposed reductions to net plant. Following Commission approval of the new depreciation rates in the March 28 order and adjustments to the Staff's proposed reductions, the Staff adjusted its projected depreciation reserve to $2,942,695,000.

In exceptions, Consumers notes that the ALJ did not make a specific recommendation regarding the appropriate balance of depreciation reserve. Consumers states that both the Staff and the company agree that the depreciation reserve should be calculated using the new depreciation rates approved in the March 28 order. However, Consumers disagrees with the Staff's proposed reductions to net plant, and argues that it sufficiently supported the amount of net plant in its briefing and exceptions. Therefore, Consumers requests that the Commission approve $2,946,486,000 as the amount of depreciation reserve.

In reply, the Staff agrees with Consumers that the ALJ did not make a recommendation regarding depreciation reserve and that the new depreciation rates should be used to calculate the correct amount. In addition, the Staff agrees with Consumers that the starting amount for the depreciation reserve should be the company's suggested $2,946,486,000, but recommends that it should be adjusted based on the Commission's decisions in this order.

Consumers and the Staff agreed that the starting amount for depreciation reserve should be $2,946,486,000. The Commission adopts the agreed-upon starting amount, which is adjusted to $2,943,867,000 based on the decisions set forth in this order.

B. Working Capital

In its initial filing, Consumers projected $652.952 million for working capital, while the Staff recommended $634.063 million, approximately $19 million less than the company's projection. After adoption and modification of the Staff's proposed adjustments, Consumers and the Staff agreed to a revised working capital balance of $642.558 million.

The Attorney General argued that Consumers' working capital should be reduced by $73.9 million as a result of his proposed adjustments to the company's cash balance, accrued taxes, and levels of interest and dividends payable.

In response, Consumers asserted that the Attorney General's proposed cash balance adjustment would leave the company with only $7 million in its working capital balance for the test year, which is only 0.4% of gas revenues. Consumers stated that its projected cash balance is necessary to address seasonal cash flows, the timing of new bond issuances, and to ensure sufficient liquidity to operate the company's large capital expenditure program.

Consumers explained that the large decrease in accrued taxes is due to an increase in the company's deferred federal income taxes (DFIT) as a result of an extension by Congress of bonus depreciation for tax years 2015-2019, and Consumers' corresponding legal duty to comply with the federal consistency requirements of the normalization rules. 6 Tr 781. In addition, Consumers recommended rejection of the Attorney General's proposed adjustment to the company's interest and dividend payable amounts because, according to Consumers, the Attorney General failed to provide evidence of the correlation between capital structure balances and interest and dividend payables.

The ALJ agreed with Consumers and recommended that the Commission reject the Attorney General's proposed adjustments to the company's 2017 cash balance, accrued taxes, and levels of interest and dividends payable. The ALJ determined that Consumers provided a sufficient explanation rebutting the Attorney General's concerns. Therefore, the ALJ adopted Consumers' revised working capital amount of $642,558,000.

No exceptions were filed, and the Commission adopts the findings and recommendations of the ALJ.

1. Calculation of Cost of Gas Sold and Gas Stored Underground

Through December 2017, Consumers projected a 13-month-average volume of working gas in storage of 125,128 million cubic feet (MMcf) and a 13-month-average cost of gas in storage of $373,350,290. The company stated that it used the average New York Mercantile Exchange (NYMEX) settlement prices for 2017, as of the first five business days of May 2016, which averaged $2.99 per million British thermal units for 2017. Consumers projected a 2017 average cost of gas sold of $3.18 per thousand cubic feet. The company stated that this price "reflects locational pricing differences between NYMEX (Henry Hub) and other supply locations (basis), transportation costs, unused reservation charges, and the [gas cost recovery] GCR accounting treatment of net system uses." 6 Tr 990.

The Staff recommended the use of a five-year average of actual gas-in-kind (GIK) volumes for "other customers." Consumers disputed the Staff's proposal, arguing that it separates the

GIK volumes from the forecasted storage and supply activities and the corresponding GIK requirements that are set forth in the existing Act 9 contracts for these customers.

The ALJ found that for the reasons set forth in the Lost and Unaccounted for (LAUF) Gas section, the Staff's proposed use of a five-year average of actual GIK volumes is reasonable and prudent.

In exceptions, Consumers requests that the Commission reject the ALJ's recommendation for the reasons set forth in the LAUF Gas section below.

The Commission adopts the findings and recommendations of the ALJ as set forth in the LAUF Gas section *infra*.

C. Unamortized Manufactured Gas Plant Balance

Consumers averred that it has 23 sites that formerly housed MGP. The company noted that the Commission previously addressed environmental investigation and remediation expenditures at these sites in Case No. U-10755, and found that these expenditures should be subject to deferred accounting, with amortization over 10 years, beginning the year after the expenditures are incurred. 5 Tr 575. Consumers stated that following a prudency review, these expenses will be included in rates, and the deferred balance would be included in rate base and earn a return.

Consumers included an average unamortized MGP balance in the company's 2017 test year of $30.1 million. However, the Staff proposed a projected unamortized MGP balance of $23.889 million, which was accepted by the company. The Commission adopts a projected unamortized MGP balance of $23.889 million.

D. Conclusion

Based on the above decisions, the Commission finds that Consumers' total jurisdictional gas rate base is $4,304,494,000 for the test year. This is comprised of a net plant amount of

$3,638,047,000, an allowance for working capital of $642,558,000, and net unamortized MGP of $23,889,000.

V. CAPITAL STRUCTURE AND RATE OF RETURN

Consumers proposed an after-tax overall rate of return of 6.17%, with an ROE of 10.60% (the company's current ROE is 10.30%), a revised permanent capital common equity ratio of 53.10% equity to 46.9% debt. The Staff recommended an overall rate of return of 5.69%, with an ROE of 9.50%, and a common equity ratio of 52.63% equity to 47.37% debt. The Attorney General recommended an overall rate of return of 5.70%, with an ROE of 9.75%, and a capital structure of 50/50 equity to debt. ABATE recommended an overall rate of return of 5.70%, with an ROE of 9.30%.

A. Capital Structure

Consumers projected an average common equity balance of approximately $6.320 billion, whereas the Staff projected approximately $6.200 billion in common equity. The Staff explained that the difference between the projections "stems from a revision to the Company's forecasted equity infusions in January 2017 and June 2017." 7 Tr 1675. The Staff argued that its recommended equity infusions account for a higher infusion amount that was received by the company in January 2017, and that they properly account for future equity requirements.

The Attorney General recommended reducing Consumers' proposed common equity balance by $341 million, and increasing the company's long-term debt balance by the same amount, to achieve a 50/50 equity-to-debt ratio. The Attorney General asserted that Consumers' debt-to-equity ratio is excessive compared to other gas utilities and that a higher level of common equity unnecessarily increases costs to customers.

Consumers responded that the Staff provided no evidence that the equity infusions were needless or excessive. Rather, the company asserted that the projected equity infusions were, in fact, accurate and timely, and are a key component of utility operations. Consumers also argued that the Attorney General's rationale for his adjustment is inaccurate and irrelevant to this case.

The ALJ agreed with Consumers and found that the company's proposed $6.320 billion common equity balance was reasonable and supported by the record. The ALJ stated that Consumers "undertook an analysis of the Company's actual expected capital needs during the test year in developing its recommended equity infusions, whereas Staff's recommendation has included no such analysis of the Company's actual capital needs and no evidence that the equity infusions were unnecessary or overstated." PFD, pp. 74-75. Similarly, the ALJ stated, the Staff provided no evidence to contradict Consumers' contention that its proposed common equity balance and equity-to-debt ratio will enable the company to maintain strong credit ratings and better withstand shocks in the financial markets, thus ensuring efficient implementation of its capital expenditure program. *Id.*, p. 75.

The ALJ also found that the Attorney General failed to provide sufficient support for his proposed adjustment and failed to provide a rationale for a 50% equity ratio. She further found that his argument that Consumers' equity balance is, at least in part, funded by long-term debt from its parent company, has been considered and rejected by the Commission. Therefore, the ALJ recommended that the Commission adopt the company's proposed common equity balance, representing a ratio of 53.10% equity to 46.8% long-term debt, and overall cost of capital of 41.27%. However, she recommended that the Commission reiterate that "in light of the Company's significant infrastructure capital investments over the next five years" and the company's "'cycle of heavier-than-usual investment,'" it will "'present an ideal opportunity to rebalance Consumers' capital structure to reach its 50/50 goal.'" *Id.*, p. 79, quoting the February 28 order, p. 64.

The Staff excepts, arguing that Consumers provided no evidence that it analyzed its actual expected capital needs during the test year. In response to the ALJ's conclusion that the Staff failed to perform a similar analysis, the Staff explains that any projection would have been speculative because the Staff has no knowledge of Consumers' upcoming capital requirements. Instead, the Staff states that its test-year equity infusion estimates are based on "*actual infusions* that the Company received over the course of its capital investments program." Staff's exceptions, p. 9 (emphasis in the original). The Staff also argues that the ALJ's recommendation to adopt Consumers' increase in its equity balance from 52.88% to 53.10% contradicts the directive in the February 28 order that the company rebalance its capital structure to reach an optimal goal of 50/50.

In exceptions, the Attorney General argues that instead of moving toward a more balanced debt-to-equity capital structure, Consumers is further increasing its equity amount, which is contrary to the Commission's expectations in the February 28 order. The Attorney General asserts that his proposed adjustment is more aligned with Consumers' stated goal of maintaining a balanced capital structure.

In reply to the Staff, Consumers argues that historical equity infusions are unrelated to the company's actual capital needs, and that the company's method of determining its common equity balance is more appropriate and accurate. Regarding the Staff's assertion that Consumers' proposed equity balance contradicts the Commission's directive in the February 28 order, the company responds that it filed this rate case seven months before the February 28 order and it would be unfair to impose those expectations in this case "when the Company had no advanced opportunity to conform to such a directive." Consumers' replies to exceptions, p. 24.

Consumers replies to the Attorney General that the company's proposed debt-to-equity ratio is, in fact, aligned with its goal of maintaining a ratio in the low 50% range, while supporting its intensive capital investment program and other financial goals. Consumers' replies to exceptions, p. 27.

The Commission adopts the findings and recommendations of the ALJ. However, the Commission notes that Consumers' proposed capital structure comprised of 53.1% equity to 46.89% debt represents a departure from its stated objective of a roughly balanced capital structure. As set forth in the February 28 order, the Commission has the discretion to adjust a company's capital structure to one that is reasonable. A common equity ratio that is unnecessarily equity-heavy burdens ratepayers because equity capital is more expensive than debt capital and carries with it the additional expense of a tax burden that is not present with debt capital. Consumers' treatment as a stand-alone company for ratemaking purposes requires it to maintain a capital structure that is evenly balanced between debt and equity. And, although Consumers asserts that a balanced capital structure is its goal, its proposed equity ratio continues to increasingly favor equity capital over debt capital at the expense of its ratepayers. Further, although the company seeks to characterize a 53.1% equity to 46.89% debt ratio as close enough to its intended goal, the Commission disagrees with Consumers that its proposed capital structure is sufficiently balanced to avoid scrutiny.

The Commission cannot overemphasize the company's responsibility to rebalance its equity and debt capital. The Commission agrees with the Attorney General that, considering the size of Consumers' capital portfolios, a few percentage point increase to the equity balance translates into an increase of millions of dollars, and may unnecessarily increase costs to customers. Although the Commission adopts the ALJ's recommendation of a common equity balance of $6.320 billion, or 53.10% of the company's permanent capital structure, Consumers shall, in its next rate case, articulate its strategy to return to a balanced capital structure and the steps it intends to take to reach its stated goal, or the Commission will have to consider using its regulatory authority to rebalance Consumers' capital structure.

There was agreement between Consumers and the Staff regarding the long-term and short-term debt balances, and the DFIT balance. The ALJ thus adopted Consumers' projected long-term debt balance of $5.544 billion, its projected short-term debt balance of $173 million, and its projected $3.133 billion deferred tax balance. The ALJ noted that Consumers and the Staff used balances for preferred stock and the job development investment tax credit (JDITC) that corresponded to balances in the historical period, with components for JDITC based on the allocation of long-term debt, preferred stock, and common equity. The ALJ did not expressly indicate whether she recommended that the Commission adopt those balances. No exceptions were filed on these issues, and the Commission adopts the balances agreed upon by the parties.

B. Cost Rates

Consumers and the Staff agreed upon a long-term debt cost rate of 4.74% and a short-term debt cost rate of 2.09%, and the ALJ recommended the adoption of these rates. The ALJ noted that Consumers and the Staff agreed to a 4.50% cost rate for preferred stock, and stated that:

> the cost rates for long-term debt, preferred stock, and common equity components of JDITC should correspond to the cost rates established for long-term debt, preferred stock, and common equity, the cost rate for other interest bearing accounts should be 3.25% . . . .

PFD, p. 107. No party filed exceptions, and the Commission adopts the ALJ's recommendations for these cost rates.

C. Return on Equity

The criteria for establishing a fair rate of return for public utilities is rooted in the language of the landmark United States Supreme Court cases *Bluefield Waterworks & Improvement Co v Public Service Comm of West Virginia*, 262 US 679; 43 S Ct 675; 67 L Ed 1176 (1923) and *Federal Power Comm v Hope Natural Gas Co,* 320 US 591; 64 S Ct 281; 88 L Ed 333 (1944). The Supreme Court has made clear that, in establishing a fair rate of return, consideration should be given to both investors and customers. The rate of return should not be so high as to place an unnecessary burden on ratepayers, yet should be high enough to ensure investor confidence in the financial soundness of the enterprise. Nevertheless, the determination of what is fair or reasonable "is not subject to mathematical computation with scientific exactitude but depends upon a comprehensive examination of all factors involved, having in mind the objective sought to be attained in its use." *Township of Meridian v City of East Lansing,* 342 Mich 734, 749; 71 NW2d 234 (1955). With these principles in mind, the Commission turns to the factors that form the basis for determining the rate of return for Consumers.

Consumers proposed an ROE of 10.60%, which is the midpoint of the company's suggested range of 10.30% to 10.90%. Consumers used a proxy group of seven regulated gas distribution companies, and estimated an ROE for each company using the capital asset pricing model (CAPM) and the empirical CAPM (ECAPM), risk premium, discounted cash flow (DCF), and comparable earnings analysis approaches. 5 Tr 437-448. Consumers considered additional factors including, current economic conditions and the impact of Consumers' proposed IRM and revenue decoupling mechanism (RDM). *Id.*, pp. 449-463. The company stated that its proposed ROE reflects the current state of the economy and capital markets; the need to continue to attract capital to finance Consumers' large capital investment program; the company's risk profile, as compared to the proxy group; established principles for setting a fair ROE; and the results of various economic models used to calculate the cost of equity. *Id.*, p. 430.

The Staff's proposed ROE of 9.50% is the midpoint of its recommended range of 9-10%. The Staff used a proxy group of seven publicly-traded natural gas utility companies based on criteria that included: (1) net plant greater than $2.0 billion, but less than $13.0 billion; (2) no less than approximately 45% or more of its revenues must derive from regulated natural gas service; (3) an investment grade rating within three notches of that of Consumers from the two primary rating agencies, Standard and Poor's and Moody's; (4) companies currently paying dividends to shareholders; and (5) and companies currently not involved in mergers or major corporate buyouts. 7 Tr 1678-1681. The Staff also relied on a risk premium model and a review of other state commission decisions authorizing natural gas utility ROEs. *Id.*, p. 1677.

The Attorney General used the proxy group offered by Consumers, but omitted one company, National Fuel Gas, because, among other reasons, "only approximately 25% of its earnings and invested capital [is] in the natural gas distribution business." 7 Tr 1315-1316. He added two other companies, Nisource and New Jersey Resources that, like the other companies in Consumers' proxy group, are from Value Line's Natural Gas Utility group. *Id.* The Attorney General applied the DCF, CAPM, and risk premium models, along with information regarding the current capital markets and other state commissions. He calculated an average cost of equity of 9.02% in this manner, but increased his recommendation to a range of 9.50% to 9.75% based on the fact that Consumers serves a territory that is highly dependent on the automotive industry, thus the cost of capital may be higher. As a result, the Attorney General recommended an ROE in the range of 9.50% to 9.75% as part of a gradual transition to the true cost of equity. *Id.*, pp. 1325-1326.

ABATE proposed an ROE of 9.30%, which is the midpoint of its recommended range of 9.20% to 9.40%. In selecting its proxy group, ABATE excluded Value Line Natural Gas Utility Industry companies that: (1) did not have an investment grade credit rating from Standard and Poor's or Moody's; (2) did not pay dividends; (3) did not have growth rate projections from Zack's, SNL Financial, and Thomson Reuters; and (4) that were involved in significant merger or acquisition activity. 7 Tr 1540. Excluding NiSource and UGI Utilities, Inc., ABATE identified a proxy group of seven companies. Exhibit AB-6. To estimate Consumers' cost of equity, ABATE used the risk premium model, CAPM analysis, a multi-stage growth DCF model, and various forms of the constant growth DCF model. 7 Tr 1540. ABATE argued that there is observable market evidence showing historically low levels of capital market costs, that authorized ROEs have fallen to the low- to mid-9.0% range, that utilities are able to access capital to fund large capital programs, and that utilities' investment-grade credit standings are stable, if not improving. *Id.*, p. 1533.

The ALJ found Consumers' proposed ROE to be excessive, and recommended that the Commission set the company's ROE at 10.00% for five reasons. First, the ALJ noted that Consumers' proposed ROE disregards the impact of the company's solid credit rating and the current low-interest-rate climate. 7 Tr 1692. Second, the ALJ found that three of the model-based analyses performed by Consumers were based on flawed assumptions. Citing testimony by the Staff, the Attorney General, and ABATE, the ALJ stated that Consumers' use of the historical risk free rate of 5.07% in its CAPM analysis is faulty because "the historical average yield distorts the accuracy of the Company's future borrowing costs and thus distorts an investor's reasonable required rate of return to invest in the Company." PFD, p. 98, citing 7 Tr 1324, 1577, and 1687. The ALJ also noted that Consumers' use of adjusted betas in its

ECAPM model was improper because the adjustment to the ROE estimate is double-counted, thus producing an improperly high result. 7 Tr 1583, 1688. And, the ALJ found that Consumers' use of company-provided long-term guidance growth rates in its DCF analysis is "inherently biased and lacking in impartiality and represents a recent departure from the Company's use of projections from the same sources as the Staff." PFD, p. 99.

Third, the ALJ stated, Consumers' proposed ROE is excessive because the evidence shows that public utility ROEs have been declining in recent years, with average authorized returns ranging from 9.45% to 10.15%. 7 Tr 1326; Exhibit AG-25; 7 Tr 1528-1529, 1595, and 1691; Exhibit S-4, Schedule D-5, p. 13; *see also*, November 19 order; December 9, 2016 order in Case No. U-17999 (December 9 order); January 31 order; and February 28 order. Fourth, the ALJ was persuaded by the Staff's testimony regarding the myriad benefits associated with 2008 PA 286 (Act 286) that serve to reduce utilities' risks, and noted Consumers' solid credit rating. PFD, pp. 101-102. Finally, the ALJ cited Consumers' requested IRM and RDM, which, if approved, practically eliminate any risk that the company will not collect its authorized revenue and authorized ROE.

Nevertheless, the ALJ found that the ROEs recommended by ABATE, the Staff, and the Attorney General of 9.30%, 9.50%, and 9.75%, respectively, would be harmful to the company's credit ratings and would send a negative signal to investors. Accordingly, the ALJ concluded, Consumers' ROE should be set at 10.00%, because "This return reflects the ceiling of Staff's recommended ROE range of 9.00% to 10.0%, a range developed based on an objectively reasonable analysis that is consistent with past Commission decisions and the requirements of *Bluefield* and *Hope*, and that acknowledges both the volatility in United States and global markets and the likelihood of rising interest rates." PFD, pp. 104-105.

In exceptions, Consumers states that the ALJ is "correct that the Company is currently operating in an artificially-low interest rate environment," but she failed to consider the undisputed evidence that interest rates are rising, and "it produces an inverse (and, in fact, an *adverse*) result on utility stock prices." Consumers' exceptions, p. 29 (emphasis in the original). Therefore, Consumers argues, if its current ROE is reduced, it will be compounded by an increase in interest rates, and that will drive the company's earned ROE "even further below reasonable levels." *Id.*, p. 30. Contrary to the ALJ's determination, Consumers asserts that its solid credit rating is, at least in part, attributable to its existing ROE of 10.30%, and that any reduction will decrease the company's credit rating.

Consumers asserts that its cost of equity analyses were not based on flawed assumptions, and states that the ALJ failed to "consider Company testimony explaining the sound factual basis for the assumptions used . . . ." Consumers' exceptions, p. 34. In addition, Consumers argues, the ALJ erred by relying on recent ROE decisions by the Commission and regulatory agencies in other states. Consumers also disagrees with the ALJ's determination that Act 286 reduces the company's business risk, thus justifying an ROE below 10.30%. Finally, Consumers argues it presented substantial and unrefuted evidence that the IRM and RDM have no impact on the company's risk profile that would support a corresponding reduction in the ROE.

In exceptions, the Staff disagrees with the ALJ's recommended ROE of 10.00%, asserting that, "Coupled with the ALJ's higher recommended equity ratio in this case, this recommendation represents approximately $35 million in additional revenue requirement." Staff's exceptions, p. 10. The Staff states that there is no record evidence showing that ABATE's, the Attorney General's, or the Staff's recommended ROEs would harm Consumers' credit ratings or send a negative signal to investors.

Regarding the ALJ's determination that the ROEs recommended by the Staff, the Attorney General, and ABATE are too low and send a negative signal to investors, the Attorney General takes exception, arguing that the ALJ's analysis is based on the vague and unsubstantiated testimony of Consumers' witness.

In exceptions, ABATE argues that the ALJ's recommended 10.00% ROE, the ceiling of the Staff's recommended range, is unreasonable, not supported by proper cost of equity analyses, and relies on a "stale and misapplied risk premium projection along with stale data which does not reflect the low-risk nature of regulated utility companies or the current market cost of equity." ABATE's exceptions, p. 5.

In replies to exceptions, Consumers reiterates that any ROE below 10.30% would result in an unjust and unreasonable return, is inconsistent with investor expectations, and would send a significant negative signal to investors.

In reply, the Staff continues to support an ROE of 9.50%.

The Attorney General continues to support an ROE of 9.75% in his replies to exceptions.

On page 6 of its replies to exceptions, ABATE argues that "an appropriate ROE in this case should not exceed 9.60%."

The Commission finds that an ROE of 10.10%, and an overall rate of return of 5.97%, will best achieve the goals of providing appropriate compensation for risk, ensuring the financial soundness of the business, and maintaining a strong ability to attract capital. The Commission agrees, in general, with the ALJ's analysis and her finding that Consumers' proposed ROE of 10.60% is excessive, and with her observation that some of the evidence supports an ROE below 10%. The Commission observes that an ROE of 10.10% is consistent with its ROE determinations in recent years. Nationally, and in Michigan, ROEs are trending downward, and

Michigan's economy has improved considerably since Consumers' last contested gas rate case. In addition, the Commission agrees with the ALJ that the IRM and RDM approved in this order reduce the company's risk.

However, the Commission is cognizant that Consumers will need continued access to capital and the ability to maintain its solid credit rating; thus, the Commission finds the Staff's proposed ROE of 9.50%, the Attorney General's proposed ROE of 9.75%, and ABATE's proposed ROE of 9.30% to be low. The Commission finds that an ROE of 10.10% appropriately balances the interests of the utility with the interests of its ratepayers, and will ensure investor interest and confidence while protecting customers from unnecessarily burdensome rates.

D. Conclusion

Based on the Commission’s findings, Consumers’ overall cost of capital is set as follows:

Description	Amount	Total Capital	Cost Rate	Weighted Cost
Long-term Debt	$ 5,543,876,000	36.21%	4.74%	1.72%
Preferred Stock	37,315,000	0.24%	4.50%	0.01%
Common Equity	6,319,568,000	41.27%	10.10%	4.17%
Short-term Debt	172,800,000	1.13%	2.09%	0.02%
Customer Deposits	30,129,000	0.20%	7.00%	0.01%
Other Interest Bearing Credits	20,522,000	0.13%	3.25%	0.00%
Deferred FIT	3,132,780,000	20.46%	0.00%	0.00%
JDITC - Long-term Debt	25,663,000	0.17%	4.74%	0.01%
JDITC - Preferred Stock	190,000	0.00%	4.50%	0.00%
JDITC - Common Equity	28,900,000	0.19%	10.10%	0.02%
Total	$ 15,311,742,000	100.00%		5.97%

VI. THROUGHPUT

Throughput is the total gas sales and transportation volume delivered to end-use customers during the test year, which is used to compute test-year revenues and to determine rate design issues.

Consumers stated that it utilized a weather-normalization process to develop the company’s 2017 forecasted gas delivery and customer levels. For the test year, Consumers forecasted total gas deliveries to "remain at historic weather normal levels of 301 [billion cubic feet] Bcf in 2015 into 2016 based on the continued level customer attachments. Over the next five years, total deliveries are projected to increase by 0.03 percent per annum to 302 Bcf by 2020. However, the growth or loss in gas deliveries is not symmetric across all classes." 6 Tr 938. The total customer count levels, according to Consumers, are projected to increase 0.97%, and over the next five years, the level is expected to increase 0.4% per annum, with most of the growth occurring in the residential class.

The Attorney General disagreed with the company's calculation, arguing that a more appropriate approach is a gas deliveries forecast based on the most recent weather-adjusted normalized actual sales for the 12-month period ended September 2016. Accordingly, he asserted, Consumers' 2017 total gas deliveries should be 309 Bcf, which when compared to the company's forecast for each rate schedule, results in incremental revenue of $14.3 million. The Attorney General recommended that the Commission reduce Consumers' revenue requirement and revenue deficiency by $14.3 million for the forecasted 2017 test year.

Consumers responded that the Attorney General's position fails to consider that "energy efficiency impacts forecasted sales, and these savings should be incorporated into the 2017 forecasted sales." 6 Tr 943. In addition, Consumers argued that the Attorney General's proposed forecast overlooks forecasted economic conditions and other expectations for the future.

The ALJ acknowledged that the Attorney General's calculations and analysis, "do indeed reveal a weakness in the Company's assumed reduction in gas deliveries of 4.7 Bcf over the 2016-2017 two-year period . . . ." PFD, p. 111. The ALJ noted that Consumers did not challenge the Attorney General's calculations or his conclusion, but rather, the company suggested that there is an inconsistency in the Attorney General's position regarding residential sales per customer. However, the ALJ contended, the company selectively evaluated the Attorney General's position, and when viewed in its entirety, there is no inconsistency. *Id.* Nonetheless, the ALJ concluded that the Attorney General's calculations and analysis do not justify rejection of Consumers' 2017 total gas deliveries forecast. The ALJ agreed with the company that the Attorney General's position "ignores economic conditions and the fact that regression model results have been accepted and approved in prior rate cases, [and] it overlooks the Company's unchallenged expectation that the calendar year 2016 weather adjusted actuals will be within 1% of the originally forecasted deliveries for 2016." *Id.*, p. 112. Therefore, the ALJ recommended that, at this time, the Commission should reject the Attorney General's proposal.

On page 17 of his exceptions, the Attorney General argues that the ALJ's reasons for rejecting his proposal are "baseless and should not be given any weight." He asserts that each case should be judged on its own merits, and it would be illogical to adopt Consumers' analysis in this case simply because the Commission approved a similar methodology in prior cases.

In reply, Consumers states that the Attorney General failed to identify the alleged flaws in the company's analysis, and failed to evaluate the reasonableness of the company's deliveries forecast in its entirety. Consumers asserts that the "Attorney General's own exhibit indicates the high degree of accuracy of the Company's gas deliveries forecast," and because the ALJ understood that accuracy is the primary concern, she recommended adoption of Consumers' gas deliveries forecast. Consumers' replies to exceptions, p. 41.

The Commission adopts the findings and recommendations of the ALJ. The Commission agrees with the ALJ that the Attorney General's position overlooks economic conditions and

Consumers' unchallenged expectation that the calendar year 2016 weather-adjusted actuals will be within 1% of the originally forecasted deliveries for 2016. Therefore, at this time, the Commission rejects the Attorney General's proposal.

VII. ADJUSTED NET OPERATING INCOME

Consumers projected total jurisdictional operating revenues of $1.704 billion, and an after-expense net operating income (NOI) of $220.222 million. After the projected $2.624 million allowance for funds used during construction (AFUDC) adjustment is applied, the company's adjusted NOI is $222.846 million. The Staff recommended an adjusted NOI of $240.742 million, which is an increase of $17.896 million from Consumers' projection.

A. Operating Revenue Forecast

1. Sales Revenue

Consumers projected test year sales revenues of $1,544,790,000, which reflects an adjustment to the projected number of qualifying residential income assistance (RIA) provision customers. The Staff projected total operating revenues of $1,545,636,000, and proposed adjustments to the company's low-income programs. Consumers and the Staff agreed that the test year transportation revenues should be projected at $62.398 million, and the test year "other gas" or miscellaneous revenues should be projected at $97.098 million.

Consumers proposed using a five-year average of historical annual RIA provision customer count for the projected test year. The Staff disagreed, asserting that a five-year average is not accurate because it fails to reflect that RIA enrollment has been declining by 6% annually since 2013. Instead, the Staff recommended that the combined customer count for RIA and low-income assistance credit (LIAC) qualifying customers be set at 69,000, which is the average for the first nine months of 2016.

Consumers agreed to the Staff's proposed adjustment to allow for the continuation of the existing RIA provision credit, along with the LIAC pilot credit, which will be made available to 17% of the company's qualifying customers. This results in 83% of qualifying RIA provision customers receiving a credit of $11.75, and 17% of these customers receiving a credit of $30.27.

However, Consumers opposed the Staff's proposed random selection of qualifying RIA provision customers. The company claimed that the Staff's proposal is contrary to the goals of the enhanced RIA provision, which is to provide more meaningful assistance to the company's most vulnerable customers.

Regarding the Staff's proposed customer count of 69,000, the ALJ found "that Staff's proposed adjustment more accurately reflects the historical data and recent trends, as set forth in the testimony of Staff's witness, Olumide Makinde, testimony that is not disputed by the Company." PFD, p. 114. The ALJ also determined that the Staff's testimony regarding proposed random selection of qualifying RIA provision customers was more persuasive. She agreed with the Staff that auto-enrollment ensures full participation in the LIAC program for its duration, whereas the company's first-come, first-serve proposal fails to provide customer awareness or incentive for the company to actively identify and enroll qualifying customers. In addition, the ALJ adopted Consumers' proposal to roll-in unused RIA/LIAC funds into future versions of the LIAC pilot because it "adequately addresses Staff's concern that such funds be excluded from the [Consumers Affordable Resource for Energy] CARE program – and, notably, Staff has not objected to this alternative." PFD, p. 116.

In exceptions, Consumers requests that the Commission reject the ALJ's recommended customer count, asserting that it is unreasonably low, and that an RIA/LIAC customer count of 75,000 more reasonably reflects the number of RIA/LIAC qualifying customers. According to Consumers, if the Staff's customer count is adopted, there will be insufficient funds collected in rates to provide a credit to all qualifying customers. However, if the company's proposed customer count is approved, Consumers contends that any unused credit amounts will be rolled-over to the CARE program or future versions of the LIAC pilot.

In reply, the Staff states that the appropriate projection of RIA/LIAC customers is not the number of qualifying customers, but those who are expected to receive the credits in the test year. Responding to the company's claim that if the Staff's proposed customer count is adopted, there will be insufficient funds to provide the credit to qualifying customers, the Staff asserts that this is a "specter of a claim" that has "potentially damaging implications." Staff's replies to exceptions, p. 30. The Staff argues that the RIA/LIAC provision is like any other rate, and Consumers should provide the RIA credit to any qualified customer. If this results in a deficiency, the Staff states, the company is free to file a rate case. In addition, the Staff notes that Consumers' proposal to roll-over unused funds is irrelevant to determining the RIA/LIAC customer count, and therefore should be rejected.

The Commission adopts the findings and recommendations of the ALJ. The Commission agrees with the Staff that the appropriate projection is not the number of qualifying customers, but the number of customers expected to receive the credit in the test year. The Commission finds that the Staff presented adequate and persuasive evidence demonstrating that the appropriate RIA/LIAC customer count is 69,000 for the projected test year. The Commission also agrees that Consumers shall roll-over any unused RIA/LIAC funds into future versions of the LIAC pilot.

No exceptions were filed regarding the ALJ's recommendation to randomly select qualifying RIA provision customers for program participation, and therefore, the Commission adopts the ALJ's recommendation on this issue.

B. Cost of Gas Sold

Consumers and the Staff agreed that the cost of gas sold should be projected at $707.543 million. The Commission agrees and adopts this projection.

C. Lost and Unaccounted for Gas and Company Use Gas

Consumers projected LAUF gas and company-use gas expenses to be $17.527 million and $913,000, respectively, for a test year total of $18.440 million. The company's proposed allowance for use and losses percentage, or GIK percentage, is 2.68% and proposed five-year average gas loss percentage is 1.83%.

The Staff recommended that Consumers use a five-year average of actual GIK volumes for "other customers." The Staff explained that over the five-year period, the "actual volumes have been consistent over this period, and the lowest volume over the period is more than 50% higher than that proposed by [Consumers]." 7 Tr 1633. In the Staff's opinion, the adjustment is proper because the company's forecasted GIK volumes are based on net monthly injections, whereas fuel credits are charged based on daily injections. In addition, because GIK volumes are meant to cover both losses and company-use gas, the Staff recommended that the transportation offset be applied to both company-use and LAUF volumes. *Id.* Acknowledging that the storage field inventory adjustments should be included in the calculation of the LAUF percentage, the Staff recommended inclusion only during periods in which the adjustments occur, consistent with the November 21, 2006 order in Case No. U-14547 (November 21 order).

ABATE opposed Consumers' proposed increase of its current GIK percentage from 1.83% to 2.68%. ABATE recommended that the percentage remain at 1.83%, and requested that the Commission direct the company to take action to begin lowering its LAUF and company-use percentages in future rate case proceedings. According to ABATE, increased maintenance and replacement of older facilities should decrease the company's level of losses, despite what Consumers' historical rate case filings have shown.

Responding to the Staff's proposed five-year average of GIK for "other customers," Consumers asserted that the proposal "disconnects these GIK volumes from the forecasted storage and supply activities and the corresponding GIK requirements per the existing 1929 Public Act 9 ("Act 9") contracts in place." 6 Tr 992. Consumers argued that its GIK forecast is based on normal weather conditions and is consistent with other rate case data inputs, such as the gas deliveries forecast. Because the Staff failed to normalize these weather events, the company contended there are unreasonable inconsistencies in the data inputs used for ratemaking. *Id.*, p. 993. In the company's opinion, the Staff's requested change has a consequential effect on other variables, such as the cost of gas sold, the cost of gas in storage, and the working capital requirement, and it is not reasonable to change the GIK forecast without incorporating the resulting impacts on other cost of gas variables. Consumers also disputed the Staff's proposal to base the GIK forecast on daily injections, arguing that "sufficient and precise information on future conditions is not available for the Company to create a daily forecast." Consumers' initial brief, p. 54.

Additionally, the company found the Staff's proposed application of a transportation volume offset against LAUF gas and company-use gas inappropriate because it ignores the fact that the GIK percentage is the additional gas volumes that transportation customers are required to deliver to Consumers' system to account for their portion of both company-use gas and losses. Consumers stated, "The Company is thus 'collecting' from Transportation customers their total allocation of used and lost fuel. This is netted out of the Company Use volumes to recognize that Transportation customers will be putting these volumes into the transportation (as opposed to storage) system. Thus, the Company's methodology is the correct way to apply these offsets." 7 Tr 1178.

In response to ABATE's request that the GIK percentage remain unchanged, Consumers stated that the current GIK percentage was established nearly seven years ago, prior to the company "taking actions to improve the accuracy of measuring line losses." 7 Tr 1196. The company asserted that its proposed 2.68% is incremental to the percentage sought in Consumers' last gas rate case, Case No. U-17882, which was 2.43%. In addition, Consumers explained that increased maintenance of infrastructure can either increase or decrease LAUF gas, and increased maintenance spending may actually result in higher measured delivery volumes at a send-out meter and increase LAUF volumes over those previously reported. *Id.*, p. 1197.

The ALJ determined that the Staff's proposed five-year average of actual GIK volumes for "other customers" is reasonable and should be adopted. The ALJ noted that the Staff's five-year average incorporates the weather variations identified by Consumers, and the company did not dispute the Staff's observation that over this same time period, the actual GIK volumes have been consistent and the lowest volume of "other GIK credits" was still 50% higher than the company's projection in this case. The ALJ opined:

> Using such an average is also reasonable where the Company's forecasted GIK volumes are based on net monthly injections and fuel credits are charged based on daily injections and, indeed, the Company recognizes that a daily forecast is not possible in the absence of sufficient information on future conditions.

PFD, p. 122. The ALJ also adopted the Staff's storage field inventory adjustments, finding them consistent with the November 21 order. However, the ALJ rejected the Staff's proposed transportation volume offset, stating that the Staff failed to adequately respond to Consumers' reasonable explanation of its methodology for applying the offsets.

Regarding ABATE's proposal to set the GIK percentage at 1.83%, the ALJ found that Consumers' proposed increase is the first increase in nearly seven years and is sufficiently supported by the record. In conclusion, the ALJ recommended that the Commission adopt the Staff's adjustment to GIK volumes, resulting in a reduction of $5,218,000 to LAUF gas and an increase of $4,795,000 to company-use gas, for a total reduction of $423,439.

In exceptions, Consumers contends that using a five-year average to determine projected GIK volumes for "other customers" is inappropriate, and that the ALJ's recommended change should not be made without incorporating the resulting impacts on other cost of gas variables. In addition, the company opposes the Staff's proposed storage inventory adjustment because the Staff's interpretation of the November 21 order is incorrect and inconsistent with the company's past practice, and it is impossible to know exactly when a loss occurs. However, Consumers concedes that it is willing to commence writing-off inventory adjustments over a five-year period during the period in which they are recognized, but requests that the company be granted permission to include losses in the periods shown on Exhibit A-17 in the immediate case and future dockets.

The Staff excepts, disputing the ALJ's determination that it did not respond to Consumers' explanation of its methodology for applying the transportation volume offsets; rather, the Staff states, the ALJ failed to address the Staff's response. Citing its testimony, the Staff asserts that "because the collection of gas through the allowance, as described by the Company, is for the purpose of reimbursing the Company for both Company use and losses, the offset should be applied to both [LAUF and company-use] volumes." Staff's exceptions, p. 12. The Staff argues that Consumers uses GIK provided by customers on the transportation system, but losses also occur on the same system. Therefore, the Staff avers, cost allocation should be based on the purpose of the GIK volumes, not the physical location.

In exceptions, ABATE maintains the positions set forth in its testimony and briefing.

In reply to exceptions, Consumers continues to support its LAUF gas and company-use gas expenses, its GIK percentage, and proposed five-year average gas loss percentage, based on the positions set forth in its testimony and briefing.

In response to Consumers' request to include losses in the periods listed on Exhibit A-17, the Staff states that the request is not consistent with the company's agreement to write-off inventory adjustments over a five-year period during the period in which they are recognized. The Staff asserts that "it would be inconsistent . . . to include all losses presented on Exhibit A-17 in subsequent general rate cases because future calculations of losses would necessarily include losses outside of the five year time frame." Staff's replies to exceptions, p. 15.

In its replies to exceptions, ABATE reiterates that the GIK percentage should remain unchanged and that Consumers should begin lowering its GIK percentage in future rate case proceedings.

The Commission agrees with the ALJ and finds the Staff's proposed five-year average of actual GIK volumes for "other customers" to be reasonable and prudent. In addition, the Commission finds that the Staff's storage field inventory adjustments are consistent with the

November 21 order. *See*, 7 Tr 1633-1634; November 21 order, p. 58. The Commission also agrees with the Staff that Consumers' request to include losses in the periods listed on Exhibit A-17 is not consistent with the company's agreement to write-off inventory adjustments over a five-year period during the period in which they are recognized.

However, the Commission disagrees with the ALJ that the Staff failed to provide a reasonable response refuting Consumers' explanation of its methodology for applying the transportation volume offsets. As the Staff stated in its exceptions, there was ample testimony explaining that the purpose of GIK is to reimburse Consumers for LAUF and company-use volumes, and therefore it is illogical to apply the offset to company-use volumes only.

Regarding ABATE's proposal to set the GIK percentage at 1.83%, the Commission agrees that Consumers' proposed increase is the first increase in nearly seven years and is sufficiently supported by the record. Therefore, the Commission finds that the adjustments result in a reduction of $5,218,000 to LAUF gas and an increase of $4,795,000 to company-use gas, for a total reduction of $423,439.

D. Other Operations and Maintenance and Expense

1. Gas Transmission and Distribution Operations and Maintenance Expense

Consumers projected its 2017 test year gas transmission and distribution O&M expense to be $224.744 million. This expense consists of, among others, gas distribution and customer operations (DCO) division expenses of $179.989 million and smart energy direct O&M benefit credit of $1.640 million. According to the company, its gas DCO expense of $179.989 million was calculated by taking the actual 2015 O&M expense of $174.808 million and adjusting for the Commission-ordered estimated meter reading disallowance in Case No. U-18002, and then applying respective inflation percentages to the 2015 adjusted actual expenses for 2016 and 2017 on a compounded basis.

The Attorney General recommended a $5.181 million reduction to Consumers' gas DCO division expense, arguing that the company failed to show that its operations require an adjustment for inflationary cost pressures, and he asserted that actual O&M expenses for the nine-month period ended September 2016 are 3% below 2015 expenses for the same period. He also suggested elimination of the smart energy direct O&M benefit credit, stating that Consumers failed to properly account for the cost savings.

Consumers responded that the Attorney General's proposed $5.181 million disallowance is unrealistic and unreasonable, asserting that it "ignores the reality of inflationary pressures that the Company has experienced and will experience over the three-year period of 2015 through 2017," and that Consumers' total 2017 gas transmission and distribution O&M expense is approximately $7 million less than the 2015 actual amount. 7 Tr 1183. The company also argued that its witness refuted the Attorney General's recommended elimination of the smart energy direct O&M benefit credit.

The ALJ found Consumers' gas DCO division expense of $179.989 million to be reasonable and prudent, citing company testimony that Consumers has a duty to ensure public and employee safety, while meeting basic customer service demands, in its delivery of natural gas to its customers, and that this work must be done in the face of rising contractual wages, increasing material costs, and other inflationary pressures. In addition, the ALJ agreed with Consumers that its witness sufficiently addressed the Attorney General's concerns about the smart energy direct O&M benefit credit.

On pages 19-20 of his exceptions, the Attorney General states that “Neither the explanation offered by the ALJ nor [Consumers’] comment support the proposed level of expenditures or negate the reasonableness of the Attorney General’s recommended adjustments” to the gas DCO expense. He argues that the record evidence shows that the company’s operations are not experiencing any inflationary cost pressures, and that the entire inflation adjustment should be removed. The Attorney General did not file exceptions regarding the smart energy direct O&M benefit credit.

Consumers replies that its gas DCO division 2017 test year O&M expense was reasonably calculated, and that the Staff has recognized and accepted the company’s explanation of inflationary pressures.

The Commission adopts the findings and recommendations of the ALJ. The Commission finds that Consumers provided adequate and appropriate testimony and exhibits supporting its gas DCO division expense and, thus, approves the 2017 projected test year expense of $179.989 million. The Attorney General did not file exceptions regarding smart energy direct O&M benefit credit, and his adjustment is therefore rejected.

2. Gas Comprehensive Storage and Gas Management Services Operations and Maintenance

Consumers projected a combined gas comprehensive storage (GCS) and gas management services (GMS) O&M expense of $27.426 million for the 2017 test year. The company explained that this expense consists of a base O&M amount of $25.826 million and a storage well-logging expense of $1.6 million.

The Staff initially recommended a $500,000 reduction to the company’s well-logging expense, but revised its recommendation, suggesting that the $1.6 million well-logging expense be approved as a capital expenditure and not O&M. The Staff stated that Consumers’ Exhibit

A-95 “proposes to include well logging assessment costs as capitalized costs when done in connection with a major rehabilitation project; thus, requiring Staff to move the expense out of O&M.” Staff’s initial brief, p. 79.

In response to the Staff, Consumers asserted that the Staff failed to completely and accurately evaluate the Gas Well Rehabilitation Project Plan (Project Plan) in Exhibit A-95. The company argued that the Staff provided no evidence that the well-logging expense is part of the rehabilitation project, rather than an on-going assessment activity.

The ALJ agreed with the Staff and determined that the $1.6 million well-logging O&M expense should be approved as a well remediation capital expenditure. The ALJ cited language from the Project Plan stating that the rehabilitation and well-logging work must be done simultaneously, and that the program is “designed to rebuild and log the riskiest well first under capital thus reducing the need for O&M expense in those years.” Exhibit A-95, pp. 5-8. The ALJ noted that based on the above language and Consumers’ plans to log approximately 60 wells in 2017, “it is difficult to conclude that the Company’s projected $1.6 million well logging O&M expense should not instead be considered a well remediation capital expenditure.” PFD, p. 129. As a result, the ALJ recommended that the Commission approve Consumers’ projected GCS base O&M amount of $25,826,000 for the test year, but adopt the Staff’s recommended $1,600,000 well-logging adjustment, reassigning the expense as a capital expenditure.

Consumers excepts, arguing that a close reading of the Project Plan shows that it will result in O&M savings because the majority of well-logging costs will be spent in the program, and that existing O&M and capital programs will continue to be tracked separately. Therefore, Consumers asserts that some of the well-logging costs continue to be operating expenses and that the ALJ’s recommendation should be rejected.

In exceptions, the Staff argues that "the $1.6 million for well logging has inadvertently been accounted for in the PFD twice, once in O&M and once in capital." Staff's exceptions, p. 13. The Staff explains that the costs for the project were already included in Consumers' proposed capital expenditures for storage field expenditures. The Staff contends that the ALJ inadvertently did not reduce Consumers' Other O&M expense for the $1.6 million well-logging O&M expense that was reassigned to capital expenditures. *Id.*

In reply, Consumers continues to argue that well-logging expense should be an O&M expense.

The Staff did not file replies to exceptions.

The Commission notes that according to the Project Plan, "the program is expected to reduce Operations and Maintenance expense by approximately $12.2 million over the 10 years," and it "is designed to rebuild and log the riskiest wells first under *capital* thus reducing the need for O&M expense in those years. However, after the program is complete well logging costs will resume at a more normal level and will need to be reintroduced into the budget." Exhibit A-95, p. 8 (emphasis added). Considering the company's plans to log approximately 60 wells in 2017 and the Project Plan language stating that the riskiest wells will be logged first under "capital," the Commission finds that the test year well-logging expense should be considered a capital expenditure. Thus, the Commission approves Consumers' projected GCS base O&M amount of $25,826,000, and finds that the company's $1.6 million well-logging expense should not be included as an O&M expense for the 2017 test year.

3. Corporate Services Operations and Maintenance

Consumers projected gas utility corporate services O&M of $28.655 million for the test year. However, the company asserted that economic development costs were inadvertently omitted from this total. Depending on whether the Commission approves or disallows economic development costs, Consumers requested that the costs should be added to, and not subtracted from, the total corporate services O&M expense.[3]

The Attorney General recommended a disallowance of $4.3 million related to the company's customer payment programs, which includes costs currently in rates for recurring card payments, and for the transfer of the Easy Pay service, small business customer payments, online payments, and payments made at direct payment offices into rates for the test year. According to the Attorney General, the disallowance is proper because Consumers is eliminating its credit card fee for the Easy Pay service, and therefore, the company's costs will be offset by a reduced uncollectible accounts expense.

In response, Consumers argued that the Attorney General's proposal is incorrect and deficient, and that he failed to provide any analysis to support his proposed disallowance. 5 Tr 585-586. The company stated that "there will be little to no impact on uncollectible accounts expense because the fee was not a barrier to payment of the customer's bill." *Id.*, p. 585. Consumers also asserted that the Attorney General's proposal would eliminate the expense currently in rates for the company's existing recurring card payment program. In addition, Consumers contended, his proposal would prevent the company from collecting any costs associated with accepting customer payments under the existing program or new payment programs.

The ALJ found that the Attorney General's analysis contained errors and that he failed to sufficiently explain his proposal. Therefore, the ALJ recommended that the Commission reject

[3] Economic development costs are addressed *infra*.

the Attorney General's proposed disallowance and approve Consumers' projected corporate services O&M expense of $28,655,000 for the test year.

In exceptions, the Attorney General recommended that the costs for the Easy Pay program be disallowed until an analysis is done to show the impact on the uncollectible expense, which he claims is consistent with Consumers' position. The Attorney General also asserted that the ALJ ignored the remainder of his analysis and reasons for excluding this expense, arguing that it showed that the program does not benefit ratepayers as a whole.

In reply, Consumers reiterates that the Attorney General's proposal is unreasonable, fundamentally flawed, and should be rejected.

The Commission adopts the findings and recommendations of the ALJ. The Commission agrees that the Attorney General's calculation for his proposed disallowance contained mathematical errors and was insufficiently supported. Therefore, the Commission rejects the Attorney General's proposed disallowance and approves Consumers' projected corporate services O&M expense of $28,655,000 for the test year.

4. Information Technology Operations and Maintenance

Consumers projected $37.774 million for IT O&M expense for the 2017 test year, which is based on a 2015 actual amount of $29.804 million, and a 2016 projected amount of $27.660 million. The company explained that the difference between the 2016 and 2017 amounts is due to "additional ongoing maintenance costs for projects that have recently been placed into production" such as Smart Energy, eServices Web Foundation, CE Website Redesign, and Two-Way Customer Communication. 4 Tr 192-193. In addition, Consumers asserted that a portion of the increase is attributed to the transfer of Gas Code Compliance IT projects to the IT Department.

The Staff recommended that Consumers' IT O&M expense be reduced by $8.499 million, based on a five-year average of actual expenses for 2011-2015, providing four reasons. First, the Staff noted that "the Board of Directors [business technology solutions] BTS expense projections have varied less than $1 million year to year, remaining close to $30 million per year since 2013." 7 Tr 1878. Second, because actual BTS O&M expenses have been historically volatile, the Staff stated that the Commission has adopted averaging as a projection methodology. Third, the Staff contended, as exemplified in the company's two most recent gas rate cases, Case Nos. U-17643 and U-17882, Consumers' projection methodology has proven to be incorrect. Finally, the Staff argued that "the Commission has historically adopted averaging as a reasonable and prudent methodology in projecting O&M expenses such as the BTS expenses because of its consistency and reliability." *Id.*, p. 1879.

The Staff's proposed disallowance of $8.499 million includes a reduction of $533,000 for the company's projected origination expense. The Staff asserted that these costs are a new subset of IT, and are highly speculative and contingent.

The Attorney General recommended a $1.5 million reduction to the operations expense, arguing that Consumers failed to adequately support the expense. In addition, the Attorney General proposed a $1.891 million reduction, contending that the company no longer plans to hire 23 new IT Department employees as forecasted for 2017, and therefore, Consumers failed to account for this avoided cost.

In response to the Staff, Consumers argued that it has consistently spent more on IT O&M than the amount projected by the Board of Directors, and therefore, the Staff's reliance on the Board's BTS O&M expense projection is misplaced. Regarding the Staff's claim that the 2011-2015 IT O&M expense was sporadic and volatile, the company asserted that the expense has varied less than 10% in four of the five years, and that the variance is because the "magnitude of these costs can vary greatly from project to project." 4 Tr 218. In addition, Consumers disagreed that its projection methodology is repeatedly inaccurate, stating that a review of the company's last five rate cases shows that Consumers spent only slightly under its projections. Finally, the company argued that the origination costs are reasonable and prudent, are incurred as part of the project selection process, and are not unique to this case, but were included in the investment category in past years.

Responding to the Attorney General, the company asserted that it adequately supported its proposed $3.3 million increase, citing testimony and a list of projects that have recently been placed into production. Consumers also disputed the Attorney General's proposed reduction based on employee counts, arguing that his proposal failed to recognize that the IT Department uses employees for both O&M and capital expenditures, and therefore, a change in employee count does not necessarily affect O&M expense.

The ALJ rejected the Staff's and the Attorney General's proposed reductions. The ALJ stated that Consumers:

> explained in detail the bases for the increased O&M expense from 2016, including the fact that all Gas Code Compliance program IT projects for 2017 are now funded in the IT Department, resulting in $4,309,000 being planned in the IT Investments category that previously would not have been concluded [sic]. Staff neither challenged the substance of [the] testimony nor offered any real analysis for the specific reductions in IT O&M spending set forth in Exhibit S-11.0.

PFD, p. 136 (footnote omitted). The ALJ also agreed with Consumers that a review of the company's last five gas rate cases reveals that the company spent only slightly under its projections. Additionally, the ALJ rejected the Staff's proposal to base the BTS expense on the Board of Directors' expense projection, finding that the company's annual budget and rate case filing serve different purposes, a point, the ALJ stated, that is acknowledged by the Commission.

The ALJ recommended rejection of the Attorney General's proposed reduction, finding that Consumers provided sufficient support for the proposed IT O&M expense, and "adequately justified its decision not to reduce its O&M expense as a result of its plans to no longer increase the number of IT employees." PFD, pp. 138-139.

In exceptions, the Staff argues that Consumers' forecast methodology is inaccurate as demonstrated in recent gas rate cases. The Staff notes that in Case No. U-17643, the company forecasted BTS expense of $33.839 million for 2015, but only spent $29.803 million. In Case No. U-17882, the Staff notes that Consumers projected BTS expense of $32.933 million, but only spent $27.633 million. In both cases, the Staff contends, the company projected higher costs "due to projects that were to be done in the future, were scheduled to be completed early, but never came to fruition." Staff's exceptions, p. 14. Furthermore, the Staff states, Exhibit S-11.0 shows that Consumers' actual BTS expense from 2011-2015 averaged $29.274 million annually, never exceeding $34 million on an annual basis. The Staff argues that if the company's projected BTS expense of $37.8 million is approved, it would be a $4 million increase over the company's highest amount of spending between 2011 and 2015.

The Staff asserts that while the ALJ found that for 2014 and 2015, Consumers overspent the Board of Directors' proposed budget by $49,000 to $4.035 million, and underspent in 2011 and 2012, she "failed to recognize that at the same time, the Company over-forecasted its actual spending by $4.035 million and $5.3 million in 2015 and 2016." Staff's exceptions, p. 15. In addition, the Staff states that the ALJ incorrectly determined that the Staff failed to offer any real analysis supporting its proposed reduction. The Staff argues that it provided testimony and Exhibits S-11.0 through S-11.4 to calculate the five-year average of actual expense, it demonstrated that Consumers' projections are inconsistent from rate case to rate case, and it relied on comparisons of projected costs to actual costs.

In exceptions, the Attorney General continues to support his proposed reductions, based on the positions set forth in his testimony and briefing.

In reply to the Staff, Consumers argues that "Projections from two rate cases are not an indication that the Company's projections are 'inaccurate' and 'inflated.'" Consumers' replies to exceptions, p. 51. The company reiterates that a comparison of the last five gas rate cases shows that Consumers spent only slightly under its projections. In response to the Staff's contention that Consumers' 2017 test year BTS expense is a $4 million increase over the company's highest spending amount between 2011-2015, Consumers asserts that it "explained that the transfer of funding for planned gas IT projects to the IT Department resulted in $4.3 million of O&M being planned in the IT Investments category that previously would have been planned in the gas business." *Id.*, p. 52. And, regarding the Staff's claim that it is unreasonable to include expenses that are higher than those built into the Board-reviewed budget, Consumers reiterates that it has consistently spent more on IT O&M than the amount in the budget, and that the Commission has denied requests to limit the company's O&M expense to the annual budget amount. *Id.*, p. 53.

Then, on page 54 of its replies to exceptions, the company states that the Attorney General "wrongly assumes that the Company should precisely quantify those costs that make up the $3.3 million increase over the 2015 actual amount. The Operations O&M expense can vary year to year, depending on the projects that are placed into production and the ongoing maintenance costs of those projects." In addition, Consumers contends that although it no longer plans to hire 23 new IT employees, labor resource requirements will be accomplished through other means, and therefore, there will not be a corresponding O&M expense reduction.

The Commission adopts the ALJ's findings and recommendations regarding the Attorney General's proposed disallowance, but finds that the Staff's proposed $8.499 million reduction should be approved. A review of Exhibits S-11.0 through S-11.4 reveals that Consumers' five-year average (2011-2015) of BTS O&M expense is $29.274 million, which is significantly less than the $37.774 million projected for the 2017 test year. As the Staff notes, in Case No. U-17643, Consumers projected BTS expense of $33.839 million for 2015, but only spent $29.803 million, and in Case No. U-17882, the company projected BTS expense of $32.933 million, but only spent $27.633 million. In its testimony, Consumers asserted that its proposed 2017 increase "reflects the additional ongoing maintenance costs for projects that have recently been placed into production." 4 Tr 192-193. However, the company failed to explain or provide project/cost detail defining the investments included in "ongoing maintenance."

The Staff argued that Consumers' projected $37.774 million is $4 million more than the company's highest spending point between 2011 and 2015. Consumers replied that the $4.3 million can be attributed to the transfer of funding for planned gas IT projects to the IT Department. The Commission reviewed Consumers' testimony and finds that although the company noted the transfer of the funding to the IT Department, the company failed to provide any detail regarding the planned gas IT projects or a breakdown of costs. Therefore, the Commission finds that Consumers did not sufficiently support its projected increase to IT O&M expense, and that the Staff's five-year average of $29.274 million is a more accurate projection of the company's 2017 test year expenses.

The Staff's proposed disallowance of $8.499 million includes a reduction of $533,000 for Consumers' projected origination expense. Consumers stated that origination expenses are not new, they are "incurred as part of the project selection process," and are important because the origination stage is “where the Company determines the technology need, identifies high-level business requirements, explores alternatives, identifies performance requirements, and invites vendors to demonstrate the effectiveness of their projects.” Consumers’ initial brief, p. 106; 4 Tr 218-219. Although Consumers provided sufficient explanation regarding the purpose of the origination expense, the Commission finds that the company failed to provide explanation and detail of how the costs were derived. Therefore, the Commission adopts the Staff’s recommended $533,000 disallowance for origination expense.

5. Pension and Benefits Expense

a. Pension Expense

Consumers projected pension plan expense of $15.542 million, and retiree health care and life insurance[4] expense of negative $6.069 million. The Staff and the Attorney General proposed a $3.369 million reduction to pension plan expense, and a $1.360 million reduction to OPEB. The Staff’s proposed pension and OPEB expense amounts were based on year-end actuarial re-measurements, which are tied to the company’s 10-K filing. The Staff recommended that Consumers be permitted to deviate from the year-end actuarial re-measurement only if the company provides written support from the actuary. In rebuttal, Consumers provided the Staff with a letter from the actuary supporting the company’s projection. As a result, the Staff adopted Consumers’ projected pension plan and OPEB expense.

The Attorney General asserted that the company’s pension expense calculation was made on June 9, 2016, using a lower discount rate of 4.06% that was “short-lived” and “no longer representative of current levels and levels expected for the 2017 test year.” Attorney General’s initial brief, pp. 19-20. Because interest rates and discount rates have returned to higher levels,

[4] Hereafter referred to as other post-employment benefits (OPEB).

the Attorney General argued that Consumers' pension expense should be based on the amount calculated on January 29, 2016, for the company's Form 10K filing.

The company responded that the Attorney General's proposal should be rejected because it was based on incorrect assumptions and data.

The ALJ determined that Consumers provided a detailed explanation of how pension and OPEB projections are made. She stated that, "except to recite Mr. Coppola's testimony in its entirety on this issue, the Attorney General has offered no argument or analysis in his initial or reply briefs," and therefore, failed to sufficiently rebut the company's testimony and evidence. PFD, pp. 141-142. As a result, the ALJ recommended rejection of the Attorney General's proposed reduction.

No exceptions were filed, and the Commission adopts the findings and recommendations of the ALJ.

b. Defined Benefit and Defined Contribution Supplemental Executive Retirement Plans

Consumers projected a defined benefit (DB) supplemental executive retirement plan (SERP) expense of $1.5 million, and a defined contribution (DC) SERP expense of $150,000. The Staff and the Attorney General recommended a disallowance of all DB SERP and DC SERP expenses, for a total disallowance of $1.650 million. Both the Staff and the Attorney General argued that the Commission has consistently excluded costs for non-qualified benefit plans as a component of the revenue requirement because "the costs of these plans are not commensurate with the benefits to ratepayers," and "the benefits of these plans accrue to investors in the form of higher share prices and dividends but benefit ratepayers only tangentially." 7 Tr 1266, 1858. The Staff noted that in the November 19 order, the Commission stated that if Consumers makes a request for recovery of expenses related to non-qualified benefit plans in future filings, the company is to include metrics quantifying the benefits to ratepayers, and provide "additional well-defined evidentiary support demonstrating that the company's total compensation (historical and test year) are, in fact, reasonable compared to peer organizations." November 19 order, p. 72.

In response, Consumers argued that DB SERP and DC SERP expenses are imperative for the company to attract, retain, and motivate an essential group of highly-skilled executives whose goal is to provide excellent, cost-effective energy and service to customers, while optimizing Consumers' resources to meet present day and future needs of the company and customers. 4 Tr 314. The company asserted that customers benefit from decisions made by these executives, including workforce and expense decisions; operational-area decisions such as safety, system reliability, improved productivity, competitive pricing, quality customer service, and financial health of the company; and employee and retiree benefits-related decisions.

The ALJ agreed with the Staff and the Attorney General, finding that the Commission has excluded this type of expense in several recent rate cases, citing the November 19 order, December 9 order, and February 28 order, and that the record in this case does not support approval of Consumers' requested DB SERP and DC SERP expenses. The ALJ found that, contrary to the Commission's directive in the November 19 order, the company failed to "provide metrics for this expense that quantifies the benefits to ratepayers," and therefore, the Staff's and the Attorney General's proposed disallowance of $1.650 million should be approved. PFD, pp. 143-144.

In exceptions, Consumers restates that the DB SERP and DC SERP benefits are a reasonable and necessary utility operating expense, and are beneficial to both shareholders and customers.

In replies to exceptions, the Staff and the Attorney General contend that the ALJ correctly found that DB SERP and DC SERP expenses should be excluded, based on the positions set forth in their testimony and briefing.

The Commission agrees with the Staff, the Attorney General, and the ALJ, and finds – as it has in the past – that this type of perquisite expense, offered to an already well-compensated category of employees, should be removed from projected pension and benefit expense. *See*, November 19 order, p. 72; December 9 order, p. 35; and February 28 order, p. 101. Consumers has failed to persuade the Commission that the expense provides benefits to ratepayers that are commensurate with its costs. 4 Tr 314-315. The Commission finds that there is no justification presented in this case to change its position on these costs, and therefore adopts the ALJ's recommendation.

c. Active Employee Health Care, Insurance, Long-term Disability Expense

Consumers projected $17.675 million for its active employee health care, life insurance, and long-term disability (LTD) insurance expense for the test year. Initially, the Staff recommended a $2.183 million reduction reflecting Consumers' 2015 actual health care expense, but subsequently supported a $500,000 downward adjustment to reflect an insurance refund. Justifying its proposed reduction, the Staff explained that: (1) for the last five years, the company's active health care costs have been trending downward; (2) due to attrition, Consumers' O&M costs were reduced by $35 million in 2014-2015; and (3) the company significantly over-projected 2015 active health care/life insurance/LTD costs in Case No. U-17882.

The Attorney General proposed reducing the expense by $2.183 million, thus aligning the expense with 2015 actual expenses, and reflecting the fact that active health care costs have declined over the past five years. He also argued that Consumers implemented cost savings measures in 2016, such as higher co-pays and deductibles, to reduce these expenses.

In response, Consumers stated that the Staff's and the Attorney General's proposed reductions should be rejected because: (1) over the last several years, the seasonal gas construction worker headcount has been increasing, thus increasing health care costs; (2) the Staff failed to account for the $2.1 million life insurance refund the company received in 2015; (3) the Staff over-estimated the impact of attrition on the O&M expense; (4) the Staff improperly relied on the theory that Consumers could see lower benefits expense through replacement of pension plans with defined benefit plans; (5) the Staff inappropriately relied on a previous rate case where projected expenses by the company were higher than what subsequently occurred; (6) numerous health care plan design changes have occurred, thus increasing health care costs; and (7) the Attorney General's calculation is not accurate because the company used more up-to-date information.

The ALJ recommended approval of the Staff's and the Attorney General's proposed $2.183 million reduction, along with the $500,000 modification noted by the Staff. Although she acknowledged Consumers' contention that the health care cost measures taken to address increasing health care expenses may not reduce expenses as in previous years, the ALJ found that "significant changes to the Company's health care plans for union and non-union employees will result in continued savings in 2016 and 2017. Along with these cost savings measures, it is undisputed that the Company's costs have gone down due to attrition – specifically, the Company expects to reduce headcount by approximately 100 employees per year." PFD, p. 146. Therefore, the ALJ recommended approval of the Staff's proposed $1,683,000 adjustment.

In exceptions, Consumers continues to support its proposed test year expense for its active employee health care, life insurance, and LTD insurance, based on the positions set forth in its testimony and briefing.

In reply, the Staff and the Attorney General continue to support their proposed reduction based on the positions set forth in their testimony and briefing.

The Commission adopts the findings and recommendations of the ALJ. The Commission agrees with the Staff, the Attorney General, and the ALJ that for the last five years, the company's active health care costs have been trending downward from $17.6 million in 2011, to $15.5 million in 2015. In addition, Consumers has informed investors that due to attrition, the company's O&M cost reductions in 2014 and 2015 were $35 million, and that continued attrition in 2016 and 2017 is expected to reduce O&M by an additional $35 million. Finally, in Case No. U-17882, Consumers projected active health care/life insurance/LTD to be $16.4 million for 2015, but actually spent $15.5 million. Therefore, the Commission finds the Staff's proposed reduction of $1,683,000 to be reasonable and prudent, and that Consumers' active health care/life insurance/LTD O&M expense for the test year is $15,992,000.

6. Employee Incentive Compensation Plan Expense

Consumers requested recovery of test year costs for incentive compensation of $6.7 million, which includes $2.0 million for its employee incentive compensation plan (EICP) and $4.7 million for its long-term incentive (restricted stock) compensation. For 2016, Consumers established 13 specific performance measures for non-officer employees which encompass safety, reliability, customer value, and financial health. Consumers anticipated that essentially the same plan goals will be in effect for 2017, with 50% of the non-officer incentive compensation based on safety, reliability, and customer value measures, and the remaining 50%

based on financial measures. 5 Tr 632-633; Exhibit A-30. However, the company stated that, "beginning with the 2016 plan the payout levels for the operational goals will be revised . . . to align the award payout level with the increased challenge in the achievement of the operating goals." *Id.*, p. 634. Consumers indicated that the goals for company officers are basically the same, but weighted differently. *Id.*, p. 635.

According to Consumers, the long-term incentive compensation plan is:

> an equity-based plan that involves issuance of restricted stock with a three-year cycle period. The long-term incentive plan has two components – a performance component (75.0 percent) and a tenure component (25.0 percent). The long-term incentive plan performance components are – relative total shareholder return ("relative TSR") and relative EPS Growth. Both are weighted equally (37.5 percent). Relative TSR compares the shareholder returns of CMS Energy to the shareholder returns of the utilities in the Standards & Poors ("S&P") 400 Midcap and in the S&P 500 indices. Relative EPS Growth compares the EPS growth of CMS Energy to the EPS growth of the utilities in the S&P 400 Midcap and in the S&P 500 indices. The performance component of the Company's long-term incentive program is based on relative TSR and relative EPS Growth because it offers a head-to-head comparison of how well the management team performed compared to other management teams in the utility industry and provides a strong line of sight to long-term strategy.
>
> The Company also awards a portion of long-term incentive compensation contingent on the basis of continued employment (referred to as "tenure" or "tenure-based"). The employee will receive stock upon remaining employed over a three-year cycle period (after being awarded the long-term incentive). The tenure-based restricted stock helps build executive share ownership, alignment with shareholder and customer interests, and serves as a talent retention mechanism.

5 Tr 617-618. Consumers argued that "The appropriate standard from a business perspective in evaluating whether the level of compensation is reasonable is whether the <u>*overall*</u> level of compensation, including both base salary and incentive compensation, is reasonable." *Id.*, pp. 642-643 (emphasis in the original). The company's witness provided lengthy testimony regarding the customer benefits of EICP and long-term incentive compensation. *Id.*, pp. 648-650. In addition, Consumers set forth a quantitative analysis of these benefits, but

acknowledged that it was difficult to quantify every metric included in the program. *Id.*, pp. 643-644. The company requested that the Commission adopt the criteria for recovery of incentive compensation costs from the 2011 Indiana Utility Regulatory Commission order involving Southern Indiana Gas and Electric Company.

The Staff recommended that the total cost of Consumers' incentive compensation plans be excluded because both the short-term and long-term plans are tied to financial metrics. Although the Commission approved rate recovery of short-term incentive compensation in the November 19 order, the Staff argued that the Commission directed Consumers, going forward, to provide "additional well-defined evidentiary support demonstrating that the company's total compensation (historical and test year) are, in fact, reasonable compared to peer organizations." 7 Tr 1854, citing November 19 order, p. 72. The Staff stated that the company failed to provide the amount of total compensation included in the projected test year, and therefore, the Staff cannot substantiate Consumers' claim that the test year total compensation is reasonable and at market median.

The Attorney General also recommended excluding all incentive compensation costs, relying on the same rationale as the Staff. However, he stated, if the Commission decides to include some of the projected incentive compensation expense in rates, it should not exceed $743,800, the amount shown by Consumers to be related only to the operating performance measures.

Consumers contended that it sufficiently responded to the Staff's concerns, that some of the information requested by the Staff is not available in the manner requested, and that the company's required achievement of financial performance, as well as operational metrics, should be deemed an added benefit for customers and not a basis for disallowance. Consumers also argued that the manner in which the Attorney General calculated his disallowance was fundamentally flawed.

The ALJ found that Consumers' EICP is based on achieving breakthrough goals related to four areas of operations: safety, reliability, customer value, and financial initiative. Within these areas, she stated, there are 13 specific performance criteria, three of which are individual performance measures for safety, three for reliability, five for customer value, and two for financial performance. The ALJ found that 50% of the non-officer incentive compensation is based on the safety, reliability, and customer value measures, and the remaining 50% is based on the financial measures. The ALJ noted that the company's witness testified about the direct customer benefits assigned to five of the metrics, and then applied a 37% allocation for gas customers, resulting in annual savings for gas customers of more than $56.910 million, which is significantly more than the annual costs of the EICP allocated to gas customers. Therefore, the ALJ recommended that the Commission adopt the portion of the company's proposed costs for its short-term EICP related to non-financial measures, which is $743,800.

The ALJ noted that, according to the Staff, the Commission had required Consumers, in the November 19 order, to provide "additional well-defined evidentiary support demonstrating that the company's total compensation (historical and test year) are, in fact, reasonable compared to peer organizations." November 19 order, p. 72. According to the ALJ, the Staff misinterpreted the Commission's order, and she found that the Commission intended the directive for DB SERP and DC SERP expenses, "which, the Commission noted, were unlike the short-term incentive compensation plan because the Commission was able to identify few, if any, metrics for the DB SERP and DC SERP expenses tied to ratepayer benefits." PFD, p. 162.

Regarding the long-term incentive compensation plan, the ALJ determined that it continues to be premised on the financial metrics of “relative total shareholder return” and “relative earns per share growth,” and she found it “difficult to understand how such an alignment of employee and shareholder interests does not incentivize the employee to make business decisions that puts the shareholders’ financial interests first.” PFD, p. 163, citing 5 Tr 617-618. The ALJ stated that there is no convincing evidence in the record showing tangible benefits to ratepayers that are commensurate with the costs of the long-term incentive compensation plan. Therefore, the ALJ recommended adoption of the Staff’s and the Attorney General’s recommended $4,700,000 disallowance for the long-term incentive compensation plan expenses.

In exceptions, Consumers reiterates the arguments set forth in its briefs, and asserts that it presented evidence that the costs of the incentive compensation plans are commensurate with the benefits to ratepayers. The company argues that “Shifting a portion of employees’ reasonable, market-based compensation to an incentive-based component <u>provides substantial benefits to customers without additional cost</u>.” Consumers’ exceptions, p. 65 (emphasis in the original). The company avers, if performance goals are not met, employees’ pay is reduced. Consumers contends that disallowing the portion of the incentive compensation costs tied to financial metrics is punitive and impedes the company’s managerial prerogative.

In exceptions and replies, the Staff and the Attorney General continue to support total disallowance of incentive compensation, based on their testimony and briefing.

In reply, Consumers continues to support full recovery of its proposed test year short-term and long-term incentive compensation costs, based on the positions set forth in its testimony and briefing.

Over the past 10 years, the Commission has rejected Consumers' proposed EICP expenses because, pursuant to the standard set forth in the December 22, 2005 order in Case No. U-14347 (December 22 order), the company failed to demonstrate that the costs to ratepayers correspond with the benefits. Incentive compensation plans that include financial metrics mostly benefit the company's investors, not ratepayers. However, as in the December 9 and February 28 orders, the Commission finds that, in this case, it is reasonable for the company to recover amounts undisputedly linked to utility operating performance metrics meant to benefit customer service.

The Commission adopts the findings and recommendations of the ALJ, finding that Consumers provided convincing evidence that the non-financial measures of the short-term EICP provide appreciable benefits to ratepayers, and the company quantified the benefits associated with the metrics of safety, reliability, and customer value. Therefore, the Commission approves recovery of $743,800 for the short-term EICP.

Regarding the long-term incentive compensation plan, the Commission agrees with the ALJ and finds that the company failed to demonstrate that the benefits to ratepayers are commensurate with the costs. Consumers' long-term incentive compensation plan is tied closely to company earnings and cash flow measurements that overwhelmingly benefit shareholders. *See*, 5 Tr 617-618. Consequently, the Commission finds, Consumers' long-term incentive compensation plan does not meet the criteria set forth in the December 22 order, and is rejected.

The Commission seeks to ensure that overall salaries and wages are reasonable and competitive, are structured in a manner that rewards improved operational performance that benefits ratepayers, and that there is adequate baseline information and transparency to inform future decisions. Thus, the Commission notes that, in an order issued today in Case No. U-18238, the Commission is approving rate case standard filing requirements. The rate case standard filing requirements contain compensation and benefits criteria. To be clear, the Commission expects a more thorough presentation of compensation levels and metrics for the company's employee compensation plans.

7. Gas Advanced Metering Infrastructure Expense

Consumers projected $2.6 million for gas AMI expense for the test year, which is comprised of $1.326 million for program management and other corporate costs allocations, and $1.264 million for the purchase and installation of gas meter modules.

The Staff recommended a test year expense of $1.974 million, asserting that Consumers has historically over-projected O&M expense for the AMI program, and on average, has only spent 76.2% of their projected expenses.

The Attorney General recommended a $736,000 disallowance based upon additional cost savings from the AMI program that are included in Exhibit A-70, but are omitted from Exhibit A-15.

In response, Consumers argued that the Staff is not claiming that the company's projection is unreasonable, but instead that Consumers overstated AMI O&M costs in two prior gas rate cases. However, the company asserted, these two prior rate cases resulted in settlement agreements and no specific amount of gas AMI cost recovery was included in rates. Therefore, Consumers contended, it is impossible for customers to overpay for something that was not included in current rates.

Responding to the Attorney General, Consumers argued that his analysis is improper because "The O&M cost amounts identified in Exhibit A-15 (SHB-3) are based on direct labor and non-labor costs, and have been appropriately adjusted for the relevant direct cost savings included in the AMI cost-benefit analysis." 6 Tr 1079.

The ALJ agreed with Consumers and found that the company provided persuasive testimony justifying the expense and adequately responding to the Staff's and the Attorney General's concerns. The ALJ stated that neither the "Staff nor the Attorney General refuted or otherwise distinguished [Consumers'] rebuttal testimony in their written submissions. In fact, Staff failed to include the recommended reduction in Staff's Initial and Reply Briefs and it could therefore be said that Staff has abandoned the issue." PFD, p. 166.

No exceptions were filed, and the Commission adopts the findings and recommendations of the ALJ.

8. Manufactured Gas Plant Direct Project Management Costs

Consumers projected $1.055 million for MGP direct project management for the test year, the Staff agreed, and therefore, the Commission adopts $1,055,000 for MGP direct project management costs.

9. Uncollectible Accounts Expense

For the test year, Consumers projected gas uncollectible expense of $20.6 million, using a three-year average of bad debt loss ratio of uncollectible accounts expense to gas service revenue for the years 2013-2015. Although the Staff and the Attorney General agreed to the company's proposed expense, Consumers suggested that the Commission take note that the Staff and the Attorney General have "taken a sharp departure" from their positions on this issue in prior cases, and requested that the Commission "weigh" this fact when considering the company's overall revenue requirement in this case. Consumers' initial brief, pp. 149-151.

The ALJ stated that she "respectfully declines to give substantive weight to the change in position by Staff and the Attorney General," and recommended that the Commission approve Consumers' proposed test year uncollectible expense. PFD, p. 168.

In exceptions, Consumers reiterates its request that the Commission consider the Staff's and the Attorney General's changed position on this issue.

In replies to exceptions, the Staff and the Attorney General assert that Consumers' projected uncollectible expense is reasonable and request Commission approval.

The Commission substantially adopts the findings and recommendations of the ALJ. The Commission agrees with the ALJ that "the Company's projected uncollectible expense amount," should be approved, however she noted that the amount was $25.3 million. PFD, p. 168. The Commission believes this was an inadvertent typographical error because the company's projected uncollectible expense amount is $20.6 million. *See*, Consumers' initial brief, p. 148; 5 Tr 571-572; Exhibit A-47 (DLH-3), pp. 1-2. Therefore, the Commission approves Consumers' projected test year uncollectible expense amount of $20,600,000.

On pages 3 and 4 of the November 14, 2013 order in Case No. U-17493, the Commission stated that "Energy assistance programs, if properly designed and executed, have the potential to not only reduce costs for and provide other benefits to participating customers, but also reduce the utility's expenses for bad debt, disconnection/reconnection, and collection activities." Therefore, with proper execution of its energy assistance programs, including the CARE pilot program, the Commission expects that a new trend is being set, leading to continued reductions in Consumers' uncollectible expense going forward.

10. Economic Development Expense

Consumers projected economic development expense of $2 million for the test year. According to the company, this expense "would support increased staffing, marketing, and other economic development activities fundamental to business attraction and expansion. Additional activities would be carried out in cooperation with other organizations engaged in economic development." 4 Tr 333. Consumers acknowledged that the Commission rejected this expense in Case No. U-17990, but requested reconsideration because, in this case, the company has provided evidence showing that economic development activities are vital to Consumers' performance as a utility, and constitute a core component of its utility customer service function.

The Staff opposed Consumers' request for several reasons: (1) Consumers failed to include performance metrics that would measure the success of the program and hold the company accountable for its spending; (2) the expense is duplicative because the State of Michigan already spends money on economic development to attract new business to the state; (3) the Commission does not permit economic development expenses in rates for any other Michigan utility, and if Consumers is provided recovery for these expenses, it will put those other utilities at an unfair disadvantage; and (4) economic development is "not a core utility function that is required to provide safe and reliable service at just and reasonable rates." 7 Tr 1849-1850.

The Attorney General agreed with the Staff that economic development is not a core function of providing utility service. In addition, he contended, "when requested to put forth some goal or target of what additional load growth the company would hope to achieve, the Company has stated that it does not have a load growth target correlated to spending the incremental $2 million funding requested." 7 Tr 1288.

Citing the Commission's decision in the February 28 order, the ALJ found that the record in this case "is similarly devoid of any demonstration by the Company that economic development is a core utility function necessary for the provision of safe and reliable service at just and reasonable rates." PFD, p. 172. In addition, the ALJ found that Consumers failed to provide a performance tool or metric to demonstrate or quantify any ratepayer benefits associated with the expense. Therefore, the ALJ recommended adoption of the Staff's and the Attorney General's proposed total disallowance of the company's projected economic development expense.

Consumers takes exception, restating that the company provided adequate evidence demonstrating that economic development costs are a core utility function. And, the company argues that its witness described in detail the customer benefits associated with Consumers' engagement in economic development activities. However, Consumers states, if the Commission disallows this expense, the company requests that economic development costs not be subtracted from its total corporate services O&M amount. Consumers asserts that the ALJ's calculated revenue deficiency improperly double-counted this disallowance.

In reply, the Staff and the Attorney General continue to support their proposed disallowance, based on the positions in their testimony and briefing. In response to Consumers' claim that the $2 million was not included in the ALJ's calculated revenue deficiency, the Staff argues that the company presented no evidence to support this claim. The Staff asserts that Consumers improperly raised this claim in rebuttal, effectively precluding the Staff from auditing the new, increased request.

The Commission agrees with the Staff, the Attorney General, and the ALJ, and finds – as it has in the past – that this type of expense is not a core utility function that is required to provide safe and reliable service at just and reasonable rates. In addition, Consumers did not provide specific performance metrics, and without substantive record evidence, the Commission is unable to measure the company's spending, the success of the program, or the benefit to ratepayers. The Commission also agrees with the Staff that Consumers did not substantiate its claim that the ALJ double-counted this disallowance.

E. Depreciation and Amortization – Non-manufactured Gas Plant

Consumers initially projected test year non-MGP depreciation expense of $218,705,000. However, in the March 28 order, revised depreciation rates were approved. Both Consumers and the Staff agreed that the application of these new depreciation rates results in a $2.974 million reduction in the company's annual non-MGP depreciation expense. The Commission agrees with Consumers and the Staff and finds that the non-MGP depreciation expense is $215,731,000. However, the expense is reduced by $3,546,000 based on the decisions set forth in this order.

F. Manufactured Gas Plan Amortization Expense

Consumers projected a $4.815 million test year MGP amortization expense, the Staff agreed, and therefore, the Commission adopts $4,815,000 for MGP amortization expense.

G. Taxes

Consumers projected test year property tax expense of $78.9 million, while the Staff calculated $77.6 million, with the difference due to the Staff's proposed adjustments to plant.

For federal income tax (FIT), Michigan Corporate Income Tax (MCIT), and local income tax (LIT), Consumers projected $56.098 million, $15.997 million, and $489,000, respectively. The Staff calculated $66.382 million for FIT, $17.841 million for MCIT, and $546,000 for LIT, with the differences due to the Staff's proposed adjustments to Consumers' projected revenue and expenses.

Regarding its other general taxes, Consumers calculated $15.054 million for the test year, and the Staff agreed.

The Commission finds Consumers' projections for test year tax expenses to be reasonable, but they are adjusted, based on other decisions set forth in this order.

H. Allowance for Funds Used During Construction

Consumers' projected AFUDC expense is $2.624 million for the test year, the Staff agreed, and therefore, the Commission adopts $2,624,000 for the company's AFUDC expense.

I. Conclusion

In light of these decisions, the Commission finds that total adjusted NOI is $238,958,000.

VIII. OTHER COST AND REVENUE ISSUES

A. Revenue Decoupling Mechanism

Consumers' proposed RDM uses the same methodology as the RDM that was approved in the April 21, 2016 order in Case No. U-17882. *See*, 6 Tr 834-835. The company stated that the reconciliation process will be filed three months after the end of the 12-month period following the projected test year, or three months following the implementation of new rates, whichever comes first.

No party challenged the reasonableness or prudence of Consumers' proposed RDM, and the ALJ recommended Commission approval. The Commission adopts the findings and recommendations of the ALJ.

B. The Infrastructure Recovery Mechanism

Consumers requested authority to implement an IRM that would allow for the recovery of the incremental 2018 and 2019 capital expenditures of six transmission and distribution programs. The company explained that the IRM includes programs recommended by the Staff: EIRP-distribution and EIRP-transmission, pipeline integrity-transmission and pipeline integrity-transmission operated by distribution, and the asset relocation-decision analysis mains and services program. However, the company's IRM proposal also includes the TED-I program, which was opposed by the Staff. Consumers claimed that "These six programs will improve deliverability, integrity, and capacity to ensure reliable service to the Company's customers, as well as ensure compliance with state and federal regulations." 6 Tr 899. According to the company, the IRM is structured to better align with DTE Gas Company's (DTE Gas) IRM to address concerns of the Staff and other intervenors.

Consumers stated that the IRM surcharge would be effective from January 1, 2018, until rates are reset in a subsequent general rate case, with a reconciliation process at the end of 2018 and 2019. The company asserted that after the Commission approves the 2019 reconciliation, the surcharge will be adjusted to reflect actual capital expenditures, and thereafter, Consumers will annually submit a reconciliation filing to adjust the surcharge to reflect the depreciated value of the capital expenditures.

1. Staff

The Staff generally agreed with Consumers' proposed IRM, however opposed inclusion of the TED-I program and the company's request for unlimited spending flexibility that would allow it to move expenditures between programs at will. Noting that the company is requesting recovery of $120.7 million in projected TED-I expenditures for the test year, the Staff explained that the program should be excluded from the IRM because Consumers "produced no documents in this case defining the scope of the work to be done in 2017-2019, has a historic [sic] spending pattern that is far below the 2017-2019 projections, and [it] is a proactive program[,] not a reactive program." 7 Tr 1834.

The Staff noted that there is conflicting information in Exhibits A-23 and A-29 regarding the company's cost of removal for EIRP-distribution and EIRP-transmission and storage. The Staff argued that Consumers failed to sufficiently explain the conflicting information, and therefore, the Staff recommended that cost of removal be excluded from the IRM in this case and reexamined in the future.

The Staff proposed an adjustment to the surcharge calculation for the transportation class so that it is on a per-customer basis, similar to that approved in the December 9 order. The Staff also advocated for 3.2% spending flexibility, equal to that approved for DTE Gas, thus setting Consumers' allowable flexibility at $4.6 million.

Consumers responded that it provided extensive testimony and evidence defining the scope work to be done in the test year and beyond, justifying inclusion of the TED-I program in the IRM. The company also opposed the Staff's alternative recommendation to reduce the amounts of the TED-I program and pipeline integrity-transmission program expenses included in the IRM.

In response to the Staff's proposed spending flexibility cap, Consumers contended that the cap would equate to a financial penalty on the company's ability to respond to emergent circumstances. In addition, the company argued that spending flexibility will not eliminate customer protection, as argued by the Staff, because the IRM is subject to additional prudency review after the planning filing.

2. Association of Businesses Advocating Tariff Equity

ABATE requested that the Commission reject Consumers' proposed IRM for several reasons. First, ABATE stated that the proposed IRM includes costs that occur after the company's 12-month test year, and thus is contrary to MCL 460.6a(1). Second, ABATE asserted that the proposed IRM improperly and inequitably shifts costs and risk from investors to ratepayers "by providing investors with accelerated recognition of specific cost and revenue adjustments in utility rates." 7 Tr 1503. Third, according to ABATE, Act 286 provides utilities with the ability to regularly file rate cases and adjust rates, and therefore, the IRM is unnecessary. Fourth, ABATE noted that in the November 19 order, the Commission found that due to the implementation of Act 286, trackers have become unnecessary, and therefore, rejected a similar IRM proposal. Finally, ABATE argued, because of the level and consistency with which Consumers tends to over-earn its authorized ROE, a tracking mechanism is unnecessary.

In response, Consumers stated that ABATE incorrectly interpreted MCL 460.6a(1) regarding the company's right to use a fully-projected test year and its ability to implement an IRM. The company also argued that its proposed IRM differs from the tracking mechanisms ABATE identified in its testimony and briefs because it is designed to align with DTE Gas' approved IRM and to address the deficiencies in the IRM rejected by the Commission in Case No. U-17735. Consumers contended that ABATE failed to provide evidence that the company has consistently over-earned its authorized ROE, and asserted that, based on its testimony, it may have under-earned its authorized ROE in the most recent 12-month period.

3. Attorney General

The Attorney General recommended that Consumers' proposed IRM, and the Staff's modified IRM, be rejected. According to the Attorney General, the Staff's modified IRM should be rejected because: (1) it "is a significant departure from the capital infrastructure replacement programs that the Commission has previously approved for SEMCO and DTE Gas;" (2) the inclusion of the asset relocation capital expenditures is unsupported by the record and inappropriately expands the scope of the IRM; and (3) the IRM "suffers the same deficiencies that have existed with the Company's proposed IRM and other broad-based infrastructure recovery mechanisms previously rejected by the Commission." 7 Tr 1352-1353. In addition, the

Attorney General stated that the Staff's modified IRM lacks a sufficient prudency and reasonableness review of the capital expenditures, the reconciliation procedure is deficient, the company's incentive to reduce capital expenditures and other costs is reduced, the IRM inappropriately shifts risk from investors to ratepayers, the IRM lacks customer protections, and the IRM surcharge will confuse customers.

Regarding the Attorney General's claim that the IRM will reduce the company's incentive to limit capital expenditures and control costs, Consumers argued that his argument ignores the reconciliation process, "which is a critical feature of the IRM" and encourages the company to control costs. Consumers' reply brief, p. 136. The company also disputed that the IRM lacks a sufficient prudency and reasonableness review, asserting that the IRM provides two opportunities for such a review.

4. Proposal for Decision

The ALJ agreed with Consumers and the Staff, and recommended approval of a modified IRM. As a preliminary matter, the ALJ noted that the Commission has approved similar surcharge mechanisms for DTE Gas and SEMCO Energy in Case Nos. U-16999 and U-16169, respectively, that cover the replacement of high risk distribution main pipeline and, for DTE Gas, a pipeline integrity program.

In support of her recommendation, the ALJ cited the Staff's testimony discussing the reasonableness of the IRM in this case:

> The IRMs that have been in place for DTE Gas and SEMCO have provided benefits to customers, while allowing the Companies to recover the prudently incurred expenses associated with the replacement of high risk pipelines and other programs that are well defined in scope. The accelerated recovery of the capital expenditures through surcharge of these programs has allowed both DTE Gas and SEMCO to increase the safety of their systems, minimize the number of active leaks on the system, and file significantly less general rate cases since their inception. This has provided their customers greater rate stability and minimized

> the costs and resources associated with regulatory proceedings. Staff believes this is important as the Consumers' gas rate payers have been subject to six base rate increase [sic] since 2010.

PFD, p. 185, citing 7 Tr 1831. The ALJ found that because the IRM will recover incremental 2018 and 2019 capital expenditures based on the 2017 test year spending amounts set in this case, the IRM does not run afoul of MCL 460.6a(1). The ALJ noted that this same concern was resolved by the Commission in the April 13, 2013 order in Case No. U-16999 (April 13 order), and the order was later affirmed by the Court of Appeals. *See*, *In re Michigan Consol Gas Co*, unpublished opinion per curiam of the Court of Appeals, issued December 11, 2014 (Docket Nos. 316141 and 316263). In addition, she found that the filing and reconciliation timelines for the proposed IRM adequately address the Attorney General's concerns. Finally, the ALJ determined that the remaining concerns of ABATE and the Attorney General were too general and lacked evidentiary support.

After finding it reasonable for the Commission to adopt an IRM in this case, the ALJ determined that most of the modifications proposed by the Staff are reasonable and should be adopted. First, the ALJ agreed with the Staff that Consumers did not present sufficient support to include the TED-I program in the IRM. The ALJ found persuasive the Staff's testimony that the company failed to provide any documents defining the scope of the work to be done in 2017-2019, the company's historical spending pattern is far below the 2017-2019 projections, and the program is proactive, and not reactive. Second, the ALJ found that pursuant to the recommendation in the pipeline integrity-transmission program section, section IV.A.1.a., above, the reduced test year expenditure of $29,559,670 should be included in the IRM. Third, the ALJ noted that Consumers did not oppose the Staff's proposed adjustment to the IRM surcharge calculation such that surcharges for the transportation class are on a per-customer basis, and are levied on both master and contiguous meters. The ALJ recommended adoption of this adjustment. Finally, although the Staff recommended a percentage-based spending cap, the ALJ determined that Consumers adequately demonstrated why a spending cap is unnecessary in this case. The ALJ found that:

> Not only are there material differences between the programs contained in the Company's IRM and that authorized in DTE Gas Company's IRM, but the primary basis for Staff's recommendation – namely, that the Company's requested flexibility would eliminate the customer protection provided by the review and approval of reasonable program spending in the planning filing – overlooks the additional prudency review to which the IRM is subjected after the planning filing.

PFD, p. 189. Therefore, the ALJ recommended adoption of the IRM with the modifications outlined above.

5. Exceptions and Replies

In exceptions, Consumers states that, "Although the Company continues to believe that the TED-I is appropriate for inclusion in the IRM, for purposes of this case, Consumers Energy is willing to accept the PFD's recommendation to exclude it for the time being." Consumers' exceptions, p. 75. And, the company accepted the ALJ's recommendations regarding the per-customer surcharges for the transportation class and the rejection of the spending cap. However, Consumers continues to disagree with the ALJ's recommendation to reduce test year pipeline integrity-transmission program spending, and argues that the spending level included in the IRM should be the company's proposed expense of $41.8 million.

The Staff argues in exceptions that Consumers should not be allowed unlimited spending flexibility. The Staff contends that the ALJ's recommendation was based on the fact that Consumers is subject to a second prudency review after the plan filing during reconciliation proceedings. According to the Staff, the "proposed scope of the reconciliation . . . is limited in scope to only compare the actual spend to planned spend. This would not open the reconciliation to a full review of individual program spending and variations occurring between programs during the IRM year." Staff's exceptions, p. 4. If the Commission permits spending flexibility, the Staff requests that the Commission allow spending flexibility only between the non-EIRP programs and continue the approved EIRP spending as a minimum spend of $75,000,000 per year.

In addition, the Staff notes that the ALJ did not address whether cost of removal should be included in the IRM. The Staff asserts that cost of removal should not be included as a separate surcharge or included in the yearly spend totals for the reconciliation proceeding because cost of removal is captured in depreciation rates.

The Staff also argues that the ALJ failed to make a recommendation regarding the Staff's proposed 13-month average for calculating the IRM revenue requirement. The Staff requests "that the Commission require the Company to utilize the 13-month average methodology in future IRM requests to ensure that the timing of the recovery of the expenditures matches the timing of the expenditures." Staff's exceptions, p. 19.

The Attorney General continues to recommend rejection of Consumers' and the Staff's proposed IRMs, based on the positions set forth in his testimony and briefing.

In exceptions, ABATE states that the ALJ's reliance on Case Nos. U-16999 and U-16169 is misplaced because both cases ended in settlement agreements and were uncontested, the cases involved different companies with different utility structures, and the IRMs in those cases were designed through negotiation and agreement. And, contrary to the ALJ's determination, ABATE argues that it did, in fact, present evidence that Consumers over-earned on its authorized ROE on a monthly basis between March 2013 and December 2015, citing testimony and exhibits in support.

In reply to the Staff, Consumers continues to dispute the Staff's proposed spending cap based on the positions set forth in its testimony and briefing. Regarding the Attorney General's recommendation to reject the company's proposed IRM, Consumers replies that the Attorney General "cites *no record evidence* . . . to substantiate the factual assertions that underlie the arguments presented in any of his briefs." Consumers' replies to exceptions, p. 69 (emphasis in the original). In the event the Commission decides to consider the Attorney General's arguments, Consumers asserts that the company presented testimony and exhibits effectively rebutting his arguments. Finally, in reply to ABATE, Consumers argues that the IRM in Case No. U-16999 was contested, briefed by the parties, and decided by the ALJ. The company states that the parties filed exceptions and replies, and the Commission issued an order approving a modified IRM in the April 16 order. Consumers notes that the April 16 order was appealed to the Court of Appeals, which upheld the Commission's decision, and the Michigan Supreme Court denied ABATE's application for leave to appeal on July 28, 2015. Therefore, Consumers argues, "There is no basis for ABATE's claim that Consumers Energy's proposed IRM in this case is 'markedly different' from the IRM approved for DTE." *Id.*, p. 74.

The Staff and the Attorney General did not reply.

ABATE continues to recommend rejection of an IRM, based on the positions set forth in its testimony and briefing.

6. Discussion

The Commission substantially adopts the findings and recommendations of the ALJ. The Commission agrees with the ALJ that it is reasonable, prudent, and lawful to adopt a modified

IRM in this case. *See*, *In re Michigan Consol Gas Co*, unpublished opinion per curiam of the Court of Appeals, issued December 11, 2014 (Docket Nos. 316141 and 316263). Like the Staff and the ALJ, the Commission finds that Consumers did not present sufficient support to include the TED-I program in the IRM because it failed to provide any documents defining the scope of the work to be done in 2017-2019, the company's historical spending pattern is far below the 2017-2019 projections, and the program is proactive, and not reactive.[5] The Commission agrees that the reduced test year expenditure of $29,559,670 for pipeline integrity-transmission should be included in the IRM. And, the Commission finds that the Staff's proposed adjustment for the transportation class should be adopted.

However, the Commission finds it appropriate to adopt the Staff's proposed spending flexibility cap of 3.2%, equal to that approved for DTE Gas in the December 9 order, thus setting Consumers' allowable flexibility at $4.6 million. Without a spending cap, the company's prudency review is less effective, there is no reconciliation of planned costs to actual costs, and ratepayers are not sufficiently protected from imprudent spending. *See*, 7 Tr 1836-1837. The Commission agrees with the Staff that $4,600,000 in spending flexibility provides Consumers with a reasonable sum, "which the Company could use to absorb prudently incurred program overages without negatively impacting other program spending." Staff's initial brief, p. 119. Additionally, the Commission finds that Consumers shall continue the approved EIRP spending as a minimum spend of $75,000,000 per year.

The Commission also agrees with the Staff that cost of removal should not be included as a separate surcharge or included in the yearly spend totals for the reconciliation proceeding

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[5] In exceptions, Consumers agreed to exclude from the IRM the TED-I program for now. However, now that the Saginaw Trail Pipeline project is moving forward, the Commission is receptive to including the TED-I program in a future IRM, so long as Consumers provides specific and adequate information and documentation supporting inclusion of the program.

because cost of removal is captured in depreciation rates. Finally, the Commission finds it reasonable to adopt the Staff's recommended 13-month average method for future IRM requests.

C. Manufactured Gas Plant Remediation-related Expenditures

Consumers identified 23 sites that formerly housed MGP, for which the company is performing required environmental remedial activities, for an expense of $34.3 million for July 2015 through December 2017. Although the Staff supported recovery of $3,535,362 for July 2015 through December 2015, the Staff recommended that Consumers' estimated 2016 and 2017 MGP environmental expenditures of $30,731,147 be excluded because these are future remedial activities not yet executed by the company, and recovery of these expenses is contrary to previous Commission orders on this issue. 7 Tr 1728-1729. Consumers agreed.

The ALJ recommended that the Commission approve recovery of $3,535,362 for MGP remediation-related expense for July 2015 through December 2015. No exceptions were filed, and the Commission adopts the findings and recommendations of the ALJ.

D. Residential Income Assistance Provision

Using an amount of low-income support equivalent to the level that is provided under the existing provision, Consumers proposed several modifications to the RIA provision: (1) participation in the customer credit should be limited to 33,000 participants; (2) the amount of monthly RIA provision credit provided to each qualified participant should be substantially increased; (3) any unused balance for the RIA provision will be rolled over and used in a subsequent year to fund additional participation by qualifying customers or fund other assistance programs such as CARE; (4) Consumers will file an annual report detailing the level of participation, the amount of dollars, or subsidy, collected through the RIA provision from other customers, and the type of assistance provided by the company and any amounts carried over into the next year; (5) participation in the RIA provision credit will be on a first-come, first-serve basis; (6) the qualifying criteria for the credit will remain the same; and (7) participation in the RIA provision credit and receipt of credits will be limited to 12 successive months.

6 Tr 859-860.

The Staff recommended four adjustments to Consumers' proposed RIA provision. First, the Staff recommended adjusting the projected qualifying RIA provision customer count from 85,000 to 69,000, arguing that 69,000 is more representative of historical data and recent trends in the program. Second, the Staff requested that Consumers continue the current RIA program along with the company's proposed modified version, the LIAC pilot, with the total number of customers enrolled in the RIA provision divided between the RIA program and the LIAC pilot in the same proportions as those approved by the Commission in Case No. U-17999. Third, the Staff recommended that LIAC pilot participants be selected at random because auto-enrollment ensures full participation in the program for its duration. Finally, the Staff opposed Consumers' proposal to roll-over any unused RIA provision/LIAC pilot funds into the CARE program.

Consumers disputed the Staff's RIA customer count of 69,000, proposing instead to use a five-year average of historical annual RIA provision customer counts. The company also opposed the Staff's proposal to select LIAC pilot participants at random. In addition, Consumers continued to support the roll-in of unspent amounts into future versions of the LIAC pilot.

The ALJ found that, as in section VII.A.1. above, the Staff's recommended modifications to Consumers' RIA provision are reasonable and should be adopted, but with the incorporation of the company's proposed roll-in of unspent amounts into future versions of the LIAC pilot. The ALJ explained that if the company's proposed customer count of 33,000 is adopted, 36,000 low-income customers, who had once received a monthly credit, would no longer receive assistance, which is an unacceptable result.

In exceptions, Consumers continues to support its enhanced RIA provision proposal, based on the positions set forth in its testimony and briefing. Consumers contends that, "if the Commission approves the Company's LIAC pilot but also wants to continue to have the lower RIA Provision credit set at the approved monthly customer charge available for an unlimited amount of qualifying low income customers, rates will need to be modified to allow for the collection of the increase in the RIA Provision subsidy associated with the uncapped portion of the RIA Provision credit." Consumers' exceptions, p. 78.

The Staff did not reply.

The Commission adopts the findings and recommendations of the ALJ. As set forth in section VII.A.1. above, the Commission finds that the Staff's recommended modifications to Consumers' RIA provision are reasonable and prudent, and should be adopted, along with the incorporation of the company's proposed roll-in of unspent amounts into future versions of the LIAC pilot.

E. Deferred City Income Taxes

In prior years, Consumers incurred an inconsequential amount of city income taxes and the company determined that it was a much too sizable and time-consuming task to track an immaterial amount. However, Consumers stated, in recent years, there have been large increases in the company's deferred city tax liabilities, and the amount has become significant. Consumers requested authority to prospectively record these taxes using the Generally Accepted Accounting Principles deferral accounting method, to record a one-time deferred income tax liability of $5.7 million, and to recognize an associated regulatory tax asset as the offset. 6 Tr 930.

Consumers also requested that the Commission "authorize the straight-line recovery of the regulatory tax asset over a 20-year period, the approximate period over which the associated book/tax differences will reverse." *Id*., p. 932.

The ALJ recommended that the Commission approve Consumers' requested accounting treatment for deferred city income taxes. No exceptions were filed, and the Commission adopts the findings and recommendations of the ALJ.

IX. REVENUE DEFICIENCY

The Commission finds that for the period ending December 31, 2017, Consumers will experience a total revenue deficiency of $29,211,000, as follows:

Rate Base	$4,304,494,000
Required Rate of Return	5.97%
Income Required	$256,795,000
Adjusted Net Operating Income	$238,958,000
Income Deficiency	$17,837,000
Revenue Conversion Factor	1.6377
Revenue Deficiency	$29,211,000

X. COST OF SERVICE AND RATE DESIGN

A. Cost of Service

1. Design Peak Day

Consistent with current practice, Consumers' cost of service study (COSS) relies on a projected design peak day. The Staff proposed that this input be changed to an historical peak day, arguing that an historical peak day is based on an actual peak day rather than a speculative one. Consumers countered that an historical peak day is based on weather that was experienced on a single day during the historical year and does not reflect weather that could occur on a future peak day. The company further argued that it is appropriate to allocate more costs to the residential class (as the design peak day does) because that rate class is more weather-sensitive than others.

The ALJ found that the Staff did not present a persuasive basis for departing from the existing practice of relying on a design peak day. PFD, p. 201. The ALJ noted that the Commission considered this issue in the May 17, 2010 order in Case No. U-15986, pp. 64-65, and rejected the historical peak day out of concern that an historical day could present warmer than normal (WTN) weather. She found that Consumers' proposal is reasonable, supported by the record, and consistent with current practice.

The Staff excepts, arguing that a design peak day makes sense for planning activities such as the GCR plan, but not for cost allocation. The Staff asserts that the historical day relies on conditions actually experienced by the system, whereas the design peak day simply assumes an 80 heating degree day. 6 Tr 821. The Staff contends that the design peak day reflects Consumers' "operational anxieties about the future." Staff's exceptions, p. 18.

Consumers replies that the historical peak day provides only a snapshot of a single day in the past, and ignores the constantly evolving nature of the gas system, operations, customer base, and customer usage patterns. 6 Tr 841. In contrast, Consumers argues, the design peak day method uses the most current data, analyses, and forecasts to estimate customer usage in light of current and expected future conditions. Consumers notes that the design peak day is key to gas purchases and supply decisions, storage design and dispatch, system operations, and capital investment and maintenance decisions. 6 Tr 822.

ABATE also replies in support of the ALJ's recommendation.

The Commission adopts the findings and recommendations of the ALJ. While the Commission has previously acknowledged that the design peak day is most appropriate for planning purposes (as opposed to cost allocation), the Commission finds that, on this record, the design peak day appears to be preferable because it "is based on an actual historical 80 heating degree day weather event," and is a "statistically-based, data driven forecast methodology [that] considers the impact of forecasted economic and physical variables." 6 Tr 821. The Commission is not persuaded, at this time, that adoption of an historical peak day would improve the validity of the COSS.

2. Uncollectible Accounts Expense Allocation

Consumers proposed to allocate uncollectible accounts expense (UAE) by rate class, noting that only 80.4% of UAE is currently allocated to the residential class even though that class is responsible for 91.5% of gross write-offs. 6 Tr 844; Exhibit A-35. Consumers proposed a UAE allocation method that apportions 92.5% of UAE to the residential class. Consumers stated that its proposal is based on a five-year weighted average of actual historical data of uncollectible gross write-offs.

The Staff and the Attorney General contended that UAE should be allocated to all customers as a general cost of doing business, because whether or not a customer pays their bill has nothing to do with how many customers share the same rate class, and there is no reason to burden others in the same rate class disproportionately with respect to the utility's overall cost of doing business.

The ALJ recommended adoption of Consumers' proposal on grounds that it represents the actual contribution of each rate class to the UAE total. PFD, p. 203. The ALJ noted that the

Commission has repeatedly considered and rejected the Staff's proposed approach in other recent rate cases based on consideration of how different classes of customers actually cause costs.

The Staff excepts, arguing that the average customer allocator is unreasonable because it is a measure of customer counts, not a measure of the UAE associated with those customers. The Staff states that:

> gross write-offs alone are not a compelling proxy for uncollectibles because it does not include an accounting of customer debts that are paid post-write-off. . . . This distinguishes the Company's proposal from that approved for DTE, which includes those post-write-off collections. *In re DTE Gas Co*, MPSC Case No. U-17999, 12/9/16 Order, p 57. The Attorney General and Staff's proposal to allocate uncollectibles based on total cost of service, plus cost of gas is reasonable in regulatory theory, and is supported by the [National Association of Regulatory Utility Commissioners] NARUC manual. 7 TR 1624. In the alternative, if the Commission does not accept Staff's allocation methodology, it should instruct the Company to record collections by class in order to facilitate the discontinuance of the improper proxy of customer counts and move to historical net write-offs.

Staff's exceptions, p. 20.

Consumers replies that allocation of UAE by average customer better aligns allocation with causation. 6 Tr 843. Consumers explains that the current allocator apportions 80.4% of this cost to the class that produces 91.5% of all the write-offs. In contrast, Consumers argues, the Staff's proposal would allocate only 73.1% of UAE to the residential class. *Id.*, p. 844. Consumers contends that its proposal is consistent with the NARUC Electric Utility Cost Allocation Manual, which defines UAE as customer-related, and that it is important to maintain consistency between electric and gas cases for the functionalization and allocation of UAE.

ABATE also replies in support of the ALJ's recommendation.

As the Commission has stated regarding UAE, "It is appropriate and consistent with regulatory ratemaking principles to directly assign such costs to the class that caused the costs." June 15, 2015 order in Case No. U-17689, p. 27. The Commission continues to believe so. *See*, November 19 order, p. 97; December 9 order, pp. 56-57; and February 28 order, p. 132. While the Commission rejects the Staff's allocation method, the Commission agrees with the Staff's recommendation regarding recordkeeping and directs Consumers to begin recording collections by class so that net write-offs by class can be calculated.

3. Storage Cost Allocation

Consumers proposed a change to the allocation of gas storage costs from the current allocation based 50% on storage capacity and 50% on peak month sales to an allocation based 100% on storage capacity. Consumers argued that a 100% storage capacity basis represents actual use of the storage system because transportation customers do not have the ability to purchase and store gas during the summer months for winter consumption, whereas sales customers do. This change would shift approximately $19.7 million of the revenue requirement from transportation customers to sales customers. ABATE supported the proposal.

The Staff and the Attorney General opposed the proposal on grounds that the gas storage system continues to be used in the same way it has been used historically, and that use involves not just storage but also support for flowing volumes of gas on peak days, and for system balancing on a daily basis.

The ALJ found that Consumers did not make a persuasive case for change. PFD, pp. 211-212. She noted that the Commission considered this issue and adopted the 50/50 allocation in the October 28, 1993 order in Case No. U-10150, the March 11, 1996 order in Case No. U-10755, and the March 27, 1997 order in Case No. U-10960, and found that Consumers has not shown that the storage system has changed or is currently used in a different way. She further recommended that any future request by Consumers to change the current allocation be accompanied by a study showing how the storage system is used across its three major functions of storage, gas flow on peak days, and daily system balancing.

Consumers excepts, again arguing that a 100% storage allocation will reflect the actual use of the system. Consumers contends that using 50% deliverability in the calculation is redundant because the storage utilization calculation already includes consideration of deliverability, and that the peak month throughput component of the 50/50 method does not address how the system is used on a daily basis. 6 Tr 846-847. Consumers asserts that each storage field is unique, and that transportation customers are subject to restrictions on their use. Consumers points out that it already uses the 100% allocation in GCR cases with the Commission's approval. Finally, it notes that it does not have the ability to measure the metering data for transportation customers on a daily basis.

ABATE also takes exception, arguing that it presented significant evidence that storage costs are caused by, and are for the benefit of, sales customers.

The Staff replies that the inclusion of the monthly limit on storage withdrawals in the company's gas storage model is not a reasonable measure of deliverability because it does not measure the customer's daily interaction with the storage system. The Staff argues that the allocation should not be changed until there is a study that classifies the storage system into its individual components of storage, deliverability, and system balancing.

ABATE replies that sales customers are not subject to restrictions in their use of the system, and that transportation customers are less weather-sensitive than sales customers.

The Attorney General replies that neither the company nor ABATE provided evidence to support the proposed change.

The Commission adopts the findings and recommendations of the ALJ. Consumers and ABATE both seek to change the status quo on this allocation, but they failed to present compelling evidence as to why a change is warranted. The Commission agrees with the Staff that the gas storage system serves more than one purpose, and that the allocation should take this into account.

4. Peak Day Demand Allocation

Consumers currently uses the average and peak (A&P) method for the allocation of fixed delivery costs. ABATE proposed changing to a peak day demand allocation method, arguing that the A&P method significantly over-allocates costs to energy-intensive customers, leading to an unfriendly business climate. ABATE argued that transportation customers provide an above average rate of return to the company, and that allocating costs based on the peak month average usage divided by the number of days in the month will better reflect the actual system design and cost of service. Exhibit AB-1; 7 Tr 1499.

Consumers responded that it does not utilize interval demand meters on the gas side, thus data on peak day demand by class is not currently available. The Staff also opposed the proposal, arguing that the A&P method accounts for system design and usage and reflects cost causation, and accords with the NARUC Gas Distribution Rate Design Manual and Commission precedent.

The ALJ found that ABATE did not make a convincing case for change. PFD, p. 215. The ALJ noted that the Commission considered and rejected ABATE's argument in the December 9 order, pp. 57-59, wherein the Commission found that a gas distribution system has to produce both peak day service and off-peak service to be economically viable.

ABATE excepts, stating that it presented substantial evidence showing that the A&P method conflicts with system design and cost causation principles. ABATE argues that Consumers' method is based on two averages, a monthly average and an annual average, and thus dilutes peak period costs, and forces transportation customers to provide above average rates of return.

In reply, Consumers reiterates that it does not currently use interval demand meters on the gas side and could not provide peak day demand by class.

The Staff replies that the A&P method incorporates consideration of both how the system is used on peak and how the system is used every other day.

The Commission adopts the findings and recommendations of the ALJ. The Commission recently analyzed this issue and stated:

> there are sound reasons for allocating some portion of demand related costs on the basis of non-peak throughput. October 28, 1993 order in Case No. U-10150, p. 96. Contrary to ABATE's assertion, the Commission does not rely on precedent simply because it is old, but because it is correct. ABATE fails to point to any factor existing today that negates the reasoning that the Commission used in that 1993 order or previous orders. A gas distribution system has to produce both peak day service and off-peak service to be economically viable. "Peak day load alone is insufficient to pay for the cost of building the plant." *Id*. As the Staff puts it, "To focus only on the peak demand services that the system provides completely ignores how the system operates every other day of the year, when customers still expect the safe, reliable delivery of natural gas.

December 9 order, p. 59. The Commission finds that ABATE's argument is not compelling and approves the use of the A&P method.

B. Rate Design

1. Residential Customer Charge

Consumers proposed an increase to the residential customer charge from $11.75 per month to $12.75 per month based on the results of its COSS, which found that the charge should be $12.82. 6 Tr 825; Exhibit A-12. The Staff and the Attorney General opposed the change and supported the status quo based on the results of the Staff's COSS, which found that the charge should be $11.62 (the Attorney General argued that the company has a revenue sufficiency in any case). Exhibit S-6, Schedule F-1.

Based on the Staff's use of the calculation method adopted by the Commission in Case Nos. U-4771 and U-4331, and again endorsed on page 66 of the December 9 order, and page 137 of the February 28 order, the ALJ recommended retention of the current monthly residential customer charge. PFD, p. 219.

Consumers excepts, arguing that its COSS is reasonable and supports a monthly charge of $12.82.

The Staff replies that the ALJ's decision is consistent with the Staff's COSS and previous Commission orders.

The Attorney General also replies in support of the ALJ's recommendation.

The Commission adopts the findings and recommendations of the ALJ. Based on the results of the Staff's COSS, the Commission is not persuaded that the residential customer charge should be increased at this time.

2. Changes to Rates XLT, LT, ST, and GS-3

The Staff proposed the following rate increases and decreases:

> 1) setting the increase to XLT, which is due a 75.5% increase according to Staff's COSS, at 25%;
> 2) setting the increase to Large Transportation (LT) class, which is due a 19.6% increase according to Staff's COSS, at 9%;
> 3) setting the increase to Small Volume Transportation (ST) class, which is due a 7% decrease according to Staff's COSS, at 0%;
> 4) setting the increase to General Service 3 (GS-3) class, which is due a 17.8% increase according to Staff's COSS, at 10%;
> 5) setting the decrease to General Service 2 class (GS-2), which is due a 7.2% decrease according to Staff's COSS, at 5%;
> 6) setting the decrease to General Service 1 class (GS-1), which is due a 4.3% decrease according to Staff's COSS, at 2.5%; and

> 7) setting the decrease to Residential, which is due a 2.1% decrease according to Staff's COSS, at 0.8%.

7 Tr 1752-1753; Exhibit A-6, Schedule F-2.2. As shown, the proposed increases and decreases among these rates do not correspond with the results of the Staff's COSS; the Staff's recommendations attempt to avoid rate shock while moving towards cost-based rates and distributing the revenue burden as equitably as possible. 7 Tr 1751-1752. The Staff acknowledged that other rate classes need to subsidize Rates GS-3, XLT, and LT to avoid rate shock for those classes, who will still see a significant increase in any case.

The ALJ recommended adoption of the Staff's proposal, on grounds that it maintains the assumed breakeven points and minimizes rate shock as much as possible, while moving rates towards the cost to serve. PFD, p. 221.

Consumers excepts, arguing that the Staff's proposal creates interclass subsidization and rates that are not cost-based. By contrast, Consumers adds, its proposal maintains the cost basis in total for each major class. 6 Tr 850-851.

ABATE also takes exception, contending that the proposed 25% increase to Rate XLT is harsh, unreasonable, and discriminatory. ABATE notes that this rate already received an increase of 8.7% as a result of the settlement in Case No. U-17882. ABATE argues that no class rate should be increased by double digits, or by more than one and one-half times the system average increase. ABATE posits that the Staff's COSS and its rate proposal violate both principles.

The Staff replies that it is attempting to minimize the rate shock that would result from cost-based rates, and notes that the proposed XLT rate is one-third of the COSS result. The Staff indicates that it would prefer to avoid subsidization, but considers it necessary to setting a reasonable rate for XLT customers.

ABATE replies that, by reducing the proposed increase for XLT customers from 75.5% to 25%, the Staff has admitted that its COSS is unreliable.

The Commission adopts the findings and recommendations of the ALJ. The Commission does not find the Staff's COSS unreliable, and seeks to move towards cost-based rates over time; but clearly the move must be gradual because gas rates are significantly skewed, as the Staff's COSS demonstrates. The Commission agrees with the Staff that this is the most reasonable course of action.

C. Tariff Issues

Consumers identified and supported proposed changes to the gas tariff book, which are summarized in Exhibit A-63 and set forth in the proposed gas tariff sheets contained in Exhibit A-12, Schedule F-5. The Staff, the Attorney General, and ABATE recommended no changes.

Unless otherwise addressed in this order, the company's proposed changes to the gas tariff book are approved.

THEREFORE, IT IS ORDERED that:

A. Consumers Energy Company is authorized to increase its retail gas distribution rates by $29,211,000 on an annual basis effective on and after August 7, 2017, via the rate design set forth in Attachment A.

B. Within 30 days of the date of this order, Consumers Energy Company shall file revised tariff sheets substantially similar to those shown in Attachment C. Due to its voluminous nature, Attachment C is not physically attached to this order and is available electronically on the Commission's website.

C. The infrastructure recovery mechanism and associated reconciliation proceedings for the enhanced infrastructure replacement programs, pipeline integrity programs, and main renewal are approved as proposed by Consumers Energy Company and as modified by this order, and the company is authorized to exercise flexibility in spending between these programs of $4,300,000 from 2018 through 2021, annually.

D. The infrastructure recovery mechanism surcharges for 2017, as set forth in Attachment B, are approved effective January 1, 2018, and January 1, 2019, as set forth in the tariff sheet.

E. No later than 90 days from the date of this order, Consumers Energy Company shall file an application for authority to conduct a self-implementation reconciliation proceeding under MCL 460.6a(1).

F. Consumers Energy Company shall amend its reporting requirements for the enhanced infrastructure replacement programs and the non-enhanced infrastructure replacement programs in Exhibit A-28 to include the reporting requirements proposed by the Commission Staff.

G. On or before April 30 each year, Consumers Energy Company shall file in this docket a compression and storage field performance report that details the prior calendar year's performance. The report shall be consistent with the information provided in Exhibit S-10.9 and the Commission Staff's additional recommendations.

H. Consumers Energy Company shall comply with the Commission Staff's proposed reporting and metrics for the Smart Energy Program.

I. Consumers Energy Company shall, in its next rate case, articulate its strategy to return to a balanced capital structure and the steps it intends to take to reach its stated goal.

J. Consumers Energy Company shall begin recording uncollectible accounts collections by class, so that net write-offs can be calculated.

K. Consumers Energy Company shall implement the low-income assistance credit pilot program as described in this order, and shall maintain the residential income assistance program, applicable to the monthly charge approved in this order.

L. Consumers Energy Company's accounting requests are approved as set forth in the order.

The Commission reserves jurisdiction and may issue further orders as necessary.

Any party desiring to appeal this order must do so in the appropriate court within 30 days after issuance and notice of this order, under MCL 462.26. To comply with the Michigan Rules of Court's requirement to notify the Commission of an appeal, appellants shall send required notices to both the Commission's Executive Secretary and to the Commission's Legal Counsel. Electronic notifications should be sent to the Executive Secretary at mpscedockets@michigan.gov and to the Michigan Department of the Attorney General - Public Service Division at pungp1@michigan.gov. In lieu of electronic submissions, paper copies of such notifications may be sent to the Executive Secretary and the Attorney General - Public Service Division at 7109 W. Saginaw Hwy., Lansing, MI 48917.

MICHIGAN PUBLIC SERVICE COMMISSION

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Sally A. Talberg, Chairman

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Norman J. Saari, Commissioner

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Rachael A. Eubanks, Commissioner

By its action of July 31, 2017.

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Kavita Kale, Executive Secretary

MICHIGAN PUBLIC SERVICE COMMISSION

Consumers Energy Company
Summary of Present and Proposed Revenue by Rate Schedule **FOR ORDER**
Total Revenue

Line No.	Description	(a) Monthly Cust. Count	(b) Annual Consumption	(c) Present Revenues	(d) Proposed Revenues	(e) Difference Revenues	(f) Difference Percent
			MMcf	$000	$000	$000	%
	Gas Sales [1]						
	Residential Service						
1	Single Family Dwelling A	1,612,077	153,127	$ 1,132,448	$ 1,155,154	$ 22,706	2.0
2	Multifamily Dwelling A-1	9,111	6,915	42,691	43,837	1,146	2.7
3	Total Residential Service	1,621,188	160,042	1,175,139	1,198,991	23,852	2.0
	General Service						
4	Small Service GS-1	113,267	22,406	146,165	145,647	(517)	(0.4)
5	Medium Service GS-2	15,111	34,671	186,804	184,233	(2,571)	(1.4)
6	Large Service GS-3	538	8,472	37,513	38,880	1,367	3.6
7	Outdoor Lighting GL	7	2	10	7	(3)	(30.5)
8	Total General Service	128,923	65,551	370,492	368,767	(1,725)	(0.5)
9	Total Gas Sales	1,750,111	225,592	1,545,631	1,567,758	22,127	1.4
	Transportation						
10	Small Transport ST	1,404	17,825	23,369	23,369	0	0.0
11	Large Transport LT	553	19,648	17,218	18,768	1,550	9.0
12	Extra-large Transport XLT	266	38,264	21,812	27,265	5,453	25.0
13	Total Transportation	2,223	75,737	62,399	69,402	7,003	11.2
14	Total Service (Delivery & Fuel)	1,752,334	301,329	$ 1,608,030	$ 1,637,160	$ 29,130	1.8
15	Additional Late Payment Charge Revenues					76	
16	Revenue increase/(decrease) due to rounding					3	
17	Total Revenue (Sufficiency)/Deficiency					$ 29,209	

Note
[1] Includes aggregate billed transportation accounts.

MICHIGAN PUBLIC SERVICE COMMISSION

Consumers Energy Company
Summary of Present and Proposed Revenue by Rate Schedule **FOR ORDER**
Delivery Revenue

Line No.	Description	(a) Monthly Cust. Count	(b) Annual Consumption	(c) Present Revenues	(d) Proposed Revenues	(e) Difference Revenues	(f) Difference Percent
			MMcf	$000	$000	$000	%
	Gas Sales [1]						
	Residential Service						
1	Single Family Dwelling A	1,612,077	153,127	$ 645,364	$ 668,070	$ 22,706	3.5
2	Multifamily Dwelling A-1	9,111	6,915	21,197	22,343	1,146	5.4
3	Total Residential Service	1,621,188	160,042	666,561	690,413	23,852	3.6
	General Service						
4	Small Service GS-1	113,267	22,406	75,029	74,512	(517)	(0.7)
5	Medium Service GS-2	15,111	34,671	82,777	80,206	(2,571)	(3.1)
6	Large Service GS-3	538	8,472	13,716	15,083	1,367	10.0
7	Outdoor Lighting GL	7	2	10	7	(3)	(30.5)
8	Total General Service	128,923	65,551	171,532	169,807	(1,725)	(1.0)
9	Total Gas Sales	1,750,111	225,592	838,093	860,220	22,127	2.6
	Transportation						
10	Small Transport ST	1,404	17,825	23,369	23,369	0	0.0
11	Large Transport LT	553	19,648	17,218	18,768	1,550	9.0
12	Extra-large Transport XLT	266	38,264	21,812	27,265	5,453	25.0
13	Total Transportation	2,223	75,737	62,399	69,402	7,003	11.2
14	Total Delivery	1,752,334	301,329	$ 900,492	$ 929,622	$ 29,130	3.2
15	Additional Late Payment Charge Revenues					76	
16	Revenue increase/(decrease) due to rounding					3	
17	Total Revenue (Sufficiency)/Deficiency					$ 29,209	

Note

[1] Includes aggregate billed transportation accounts.

MICHIGAN PUBLIC SERVICE COMMISSION

Case No.: U-18124
Attachment A

Consumers Energy Company
Summary of Present and Proposed Rates by Rate Schedule **FOR ORDER**

Line No.	Description	(a) Units	(b) Present	(c) Proposed	Description	(d) Units	(e) Present	(f) Proposed
1	Residential Class				Transportation			
2	Single Family Dwelling A				Small Transport ST			
3	Customer Charge	$/Mth	11.75	11.75	Customer Charge - Master	$/Mth	680.20	$669.00
4	Income Assistance	$/Mth	(11.75)	(11.75)	Customer Charge - Contiguous	$/Mth	-	53.00
5	LIAC	$/Mth		(30.27)	Distribution Charge	$/Mcf	1.0285	1.0070
6	Distribution Charge	$/Mcf	2.7937	2.9594				
7					Large Transport LT			
8	Multifamily Dwelling A-1				Customer Charge - Master	$/Mth	3,644.70	$2,216.71
9	Customer Charge	$/Mth	11.75	11.75	Customer Charge - Contiguous	$/Mth	-	53.00
10	Excess Peak Charge	$/Mcf	0.0715	0.0715	Distribution Charge	$/Mcf	0.6728	0.8213
11	Distribution Charge	$/Mcf	2.7937	2.9594				
12					Extra-large Transport XLT			
13	General Service				Customer Charge - Master	$/Mth	9,732.70	$7,491.00
14	Small Service GS-1				Customer Charge - Contiguous	$/Mth	-	53.00
15	Customer Charge - Master	$/Mth	13.58	14.00	Remote Meter Charge	$/Mth	70.00	70.00
16	Customer Charge - Contiguous	$/Mth	-	14.00	Distribution Charge	$/Mcf	0.5250	0.6930
17	Distribution Charge	$/Mcf	2.5250	2.4763				
18					Authorized Tolerance Level			
19	Medium Service GS-2				6.5% ATL	$/Mcf	(0.0532)	(0.0766)
20	Customer Charge - Master	$/Mth	21.65	$49.00	7.5% ATL	$/Mcf	(0.0266)	(0.0383)
21	Customer Charge - Contiguous	$/Mth	-	41.95	8.5% ATL	$/Mcf	-	-
22	Distribution Charge	$/Mcf	2.2744	2.0571	9.5% ATL	$/Mcf	0.0266	0.0383
23					10.5% ATL	$/Mcf	0.0532	0.0766
24	Large Service GS-3							
25	Customer Charge - Master	$/Mth	632.10	$669.00	Other Transportation			
26	Customer Charge - Contiguous	$/Mth	-	53.00	Authorized Gas Use Charge	$/Mcf	1.00	1.00
27	Distribution Charge	$/Mcf	1.1811	1.3132	Unauthorized Gas Use Charge	$/Mcf	10.00	10.00
28					Load Balancing Charge	$/MMBtu	0.25	0.25
29	Outdoor Lighting GL				EUT Gas In Kind	%	1.83	2.68
30	Single Mantle	$/Lum.	11.00	7.00				
31	Multiple Mantle	$/Lum.	19.00	15.00				
32								
33	Customer Attachment Program							
34	Discount Rate	%	7.72	7.59				
35	Carrying Cost Rate	%	11.12	11.02				

MICHIGAN PUBLIC SERVICE COMMISSION

Case No.: U-18124
ATTACHMENT B

Consumers Energy Company
Calculation of Proposed Investment Recovery Mechanism Surcharge **FOR ORDER**
Year 2018 and 2019

Line No.	Description	(a) Test Year Customers	(b) Test Year Consumption	(c) 2018 IRM Revenue Requirement	(d) 2019 IRM Revenue Requirement	(e) 2018 IRM Surcharge	(f) 2019 IRM Surcharge
		#	MMcf	$000	$000	$/customer	$/customer
Gas Sales Per Customer IRM Monthly Charge							
1	Residential Service	1,621,188	160,042	13,489	26,720	$ 0.69	$ 1.37
2	Small Service GS-1	113,267	22,406	1,517	3,005	$ 1.12	$ 2.21
3	Medium Service GS-2	15,111	34,671	1,637	3,244	$ 9.03	$ 17.89
4	Large Service GS-3	538	8,472	323	639	$ 49.95	$ 99.01
5	General Service [(1)]	128,916	65,549	3,476	6,888		
						Master/Contig	Master/Contig
Transport Volumetric IRM Monthly Charge						$/customer	$/customer
6	Small Transport ST	1,404	17,825	440	873	$ 26.14	$ 51.79
7	Large Transport LT	553	19,648	386	765	$ 58.17	$ 115.29
8	Extra-large Transport XLT	266	38,264	675	1,337	$ 211.35	$ 418.98
9	Transportation	2,223	75,737	1,501	2,975		
10	Total Service	1,752,327	301,327	$ 18,466	$ 36,583		

(1) Excludes Rate GL

(Continued From Sheet No. C-23.00)

C4. APPLICATION OF RATES (Contd)

C4.7 Aggregation of Accounts (Contd)

Option A: Contiguous Facilities (Contd)

B. The building or parts of buildings, separated by a public street or alley (but not including a limited-access highway), are situated upon parcels of land which occupy wholly or in part immediately opposite street frontages on the same street or alley and are exclusively occupied and used by the customer as a unitary enterprise at one location and under one management.

C. The facility designated as the master account shall be subject to and billed under the provisions of its General Service Rate Schedule or Transportation Rate Schedule and will pay the master customer charge and the applicable distribution charge or transportation rate. Facilities designated as contiguous to the master account will pay the contiguous customer charge and the applicable distribution charge or transportation rate in effect for its General Service Rate Schedule or Transportation Rate Schedule.

Option B: ***Non-Contiguous Facilities***

A customer receiving gas service at multiple facilities under a common ownership may elect to aggregate the quantities of gas supplied to such facilities if the following conditions are met:

A. The customer must designate one of the facilities as the master account. The master account must be a transportation account under Rate ST, LT, or XLT.

B. Only subsidiary accounts will be eligible for aggregation with the master account. To qualify as a subsidiary account, a facility must be served under a sales service Rate Schedule (Rate A, A-1, GS). The customer must specify which of the other facilities will be designated as a subsidiary account.

C. The facility designated as the master account shall be subject to and billed under the provisions of its transportation tariff. Facilities designated as subsidiary accounts shall be subject to all the terms and conditions of the master account tariff, except that the subsidiary accounts will pay the customer charge and distribution charge in effect for their designated sales rates rather than the customer charge and transportation charge in effect for the master account.

C5. CUSTOMER RESPONSIBILITIES

C5.1 Access to Customer's Premises

The Company's authorized agents shall have access to the customer's premises at all reasonable hours, to install, inspect, read, repair, relocate or remove its meters; to install, operate, maintain, relocate and remove other Company property, and to inspect and determine the load characteristics of appliances installed on the customer's premises. Neglect or refusal on the part of the customer to provide reasonable access shall be sufficient cause for shutoff of service by the Company, and assurance of access may be required before service is restored.

C5.2 Bills and Payments

A. Billing Frequency

Bills for gas service shall be rendered on approximately a monthly basis, and shall be due and payable on or before the due date shown on each bill.

(Continued on Sheet No. C-24.00)

(Continued From Sheet No. C-26.00)

C5. CUSTOMER RESPONSIBILITIES (Contd)

C5.3 Restoration of Service (Contd)

Where service has been shut off for reasons as outlined in Rule C1.3, Use of Service, a meter relocation charge, if applicable, and assessed in accordance with Rule B2, Consumer Standards and Billing Practices for Electric and Gas Residential Service, R 460.116, Meter Accuracy, Meter Errors, Meter Relocations, R 460.144, Restoration of Service, and with Rule B4, Billing Practices Applicable to Non-Residential Electric and Gas Customers, R 460.1611, Meter or Facilities Relocation Charge, shall be collected from the customer whose service was shut off. The Company shall charge the customer for relocating the meter, based on the Company's current cost.

The restoration charge and meter relocation charge, if applicable, shall be billed to the customer and shall be paid before service is restored.

An On-Premises ***Site Visit*** Charge of $15.00 shall be assessed to the customer if a Company employee is sent to the premises to either serve the customer with a shut-off notification or to shut off service, unless the customer presents evidence that reasonably indicates the claim has been satisfied or is currently in dispute. The charge ***shall be applied*** to the customer account. The Company shall not assess this fee twice on the same notice for shutoff.

In the case of shutoff of service, the Company shall restore service only after the customer has paid all applicable charges authorized by its Gas Rate Book, subject to the customer's right to dispute such charges as set forth in Rule B2, Consumer Standards and Billing Practices for Electric and Gas Residential Service, and Rule B4, Billing Practices Applicable to Non-Residential Electric and Gas Customers.

C5.4 Shutoff Protection Plan for Residential Customers

A. Eligibility

Eligible low-income customers and senior citizen customers may choose to participate in the Shutoff Protection Plan (SPP) in lieu of the applicable Winter Protection Plan as described in Rule B2., Consumer Standards and Billing Practices for Electric and Gas Residential Service, R 460.148, Winter Protection Plan for Low-income Customers, or R 460.149, Winter Protection Plan for Senior Citizens. For purposes of this Company rule, an eligible low-income customer means a utility customer who has not had more than one default condition on the SPP in the last twelve months and whose household income does not exceed 200% of the federal poverty guidelines as published by the United States Department of Health and Human Services or who receives supplemental security income or low-income assistance through the Department of Human Services or successor agency, food stamps, or Medicaid. In addition, an eligible senior citizen customer means a utility customer who has not had more than one default condition on the SPP in the last twelve months, is 65 years of age or older, and advises the utility of his or her eligibility. An eligible customer enrolled in the SPP shall be referred to as an SPP Customer. Customers who are actively participating in the Consumers Affordable Resource for Energy (CARE) Pilot or have participated in the CARE Pilot during the concurrent heating season are not eligible to participate in SPP until the beginning of the next heating season. Customers may become eligible for a modified SPP as provided for in Rule C5.4. B.

(Continued on Sheet No. C-27.10)

(Continued From Sheet No. C-33.00)

C8. CUSTOMER ATTACHMENT PROGRAM

A. Purpose

The Company proposes to make extension of its gas mains and/or service lines from time to time, at its own cost, to serve applicants whose requirements will not disturb or impair the service to prior users or will not require an expenditure out of proportion to the revenue obtainable therefrom.

The Company reserves the right to delay or deny a request for service under this rule, if fulfilling such a request could, in the Company's opinion, create conditions potentially adverse to the Company or its customers. Such conditions may include, but are not limited to, safety issues, system operating requirements or capital constraints. The provisions under this Rule are in addition to the existing rules and tariffs for customer gas service.

When relocation or modification of Company facilities to an existing structure with gas service is requested or made necessary by the customer, all costs for the relocation or modification shall be charged to the requesting party.

B. Customer Contribution

A customer contribution shall be required totaling the following components: Connection Fee, any Revenue Deficiency, any Excessive Service Line Fee, and any Direct Charges. Direct Charges include, but are not limited to, any specific license fees, inspection fees, or rights of way fees charged by any political subdivision for any construction provided under this rule, and are to be paid directly to the Company. Direct charges shall also include an additional charge per foot for winter construction of all underground construction as installed, excluding conduit, applied to projects constructed during the period of December 15 to April 15, for installation of distribution or service facilities. This charge shall be based on periodic reviews of actual costs by the Company.

Any written communication from the Company regarding construction activity and its associated contribution due from the customer, unless specified otherwise in the document, shall have an expiration date of 60 days from the date issued. If either the customer or the Company takes no action by that time, the Company shall have the right to withdraw the proposal or modify the conditions under which it was made.

The Company, at its sole discretion, may waive fees or extend the service line limit for attaching parties located at the Company's storage fields or gas well locations based on the economics of a proposed project, when provided for in writing by the Company. ***The Company, at its sole discretion, may also waive in writing, fees for select attaching parties or projects where work conditions or site conditions enable efficient construction and resource deployment which permit the Company to not incur certain costs.***

C. Payment of Customer Contribution

The Connection Fee, Direct Charges and the Excessive Service Line Fee are payable in lump sum prior to construction. The Company may choose to collect these charges after construction, but prior to the meter being set, when it allows the Company to better align the construction schedule with the customers' desired service dates. The Connection Fee is non-refundable. The Direct Charges and Excessive Service Line Fee are refundable if the service line has not been installed. If the service line has been installed, the Direct Charges and Excessive Service Line Fees are non-refundable.

Unless otherwise stated by the Company, the customer shall pay any remaining charges resulting from a Revenue Deficiency in a lump sum in advance of the facility expansion. Customers deemed by the Company to require significant investment for unpredictable operations may enter into a contract with the Company to have all or a portion of the revenue deficiency designated as a deposit subject to refund, at the option of the Company. Refunds shall not exceed the amount of the deposit, and shall be based solely on any incremental increase in consumption and accompanying revenues above that recognized in the Model to calculate the customer contribution.

(Continued on Sheet No. C-35.00)

(Continued From Sheet No. C-36.00)

C8. CUSTOMER ATTACHMENT PROGRAM (Contd)

I. Model Assumptions

Incremental Revenues:

The incremental revenues will be calculated based on current rates and a forecast of the timing and number of customer attachments as well as the customers annual consumption levels.

Incremental Costs:

(1) Carrying Cost Rate

The carrying cost rate will be based on the weighted rate of debt, preferred stock, equity and associated taxes. The cost will be equal to and weighted in proportion to those authorized in the Company's most recent rate order. The carrying cost rate is equal to ***11.02%****.*

(2) Plant in Service

Plant in Service shall reflect the Company's estimated cost to construct distribution mains, customer service lines, meters and pressure regulators or regulating facilities for the Project. The timing of the facility investment, primarily service lines, will correspond with the projected timing of the customer attachments.

(3) Carrying Costs

The Carrying Costs will be the product of the average of beginning and end-of-year net plant, Plant in Service minus accumulated depreciation minus deferred taxes, multiplied by the Carrying Cost Rate, noted in paragraph 1 above.

(4) Depreciation

Depreciation expense will be the product of Plant in Service multiplied by the appropriate prescribed depreciation rates approved for the Company.

(5) Property Taxes and Other Operating Expenses

Property taxes will be the product of Plant in Service multiplied by the Company's average property tax rate. All other incremental operating expenses will be included as identified. Incremental O&M will at a minimum include a proportional cost for monthly meter reading, billing and mailing.

(6) Discount Rate

The discount rate will be a weighted rate of long-term debt, preferred stock and common equity. The cost will be equal to and weighted in proportion to those authorized in the Company's most recent rate order. Based on the Company's rate order in Case No. ***U-18124****,* the discount rate is equal to ***7.59%****.*

J. Customer Attachment Project Areas

All gas sold in any area specifically listed below is subject to the following Customer Attachment Project (CAP) charges. CAP areas and charges shall be added to or removed from the list from time to time by the Company.

(Continued on Sheet No. C-38.00)

This sheet has been cancelled and is reserved for future use.

M.P.S.C. No. 2 - Gas **Sheet No. D-1.30**
Consumers Energy Company

INVESTMENT RECOVERY MECHANISM (IRM) SURCHARGE

Rate Schedule	***IRM Surcharge (Case No. U-18124) Effective for the January 2018 Billing Month through the December 2018 Billing Month***	***IRM Surcharge (Case No. U-18124) Effective for the January 2019 Billing Month through the December 2019 Billing Month***
Rate A	***$ 0.69/customer***	***$ 1.37/customer***
Rate A-1	***0.69/customer***	***1.37/customer***
Rate GS-1	***1.12/customer***	***2.21/customer***
Rate GS-2	***9.03/customer***	***17.89/customer***
Rate GS-3	***49.95/customer***	***99.01/customer***
Rate GL	***NA***	***NA***
Rate ST	***26.14/customer***	***51.79/customer***
Rate LT	***58.17/customer***	***115.29/customer***
Rate XLT	***211.35/customer***	***418.98/customer***
Rate CC	***Per applicable distribution Rate Schedule***	***Per applicable distribution Rate Schedule***

(Continued From Sheet No. D-6.00)

RATE CATEGORIES (Contd)

Description	Rate Category
GENERAL SERVICE OUTDOOR LIGHTING RATE GL - Commercial	048
TRANSPORTATION SERVICE RATE	
Small, Cost-Based	ST
Large, Cost-Based	LT
Extremely Large, Cost-Based	XLT
CUSTOMER CHOICE RATE CC	CC

RESIDENTIAL SERVICE RATE A

Availability

Subject to any restrictions, this rate is available to any customer desiring gas service for any usual residential use in private family dwellings; tourist homes, rooming houses, dormitories, nursing homes and other similarly occupied buildings containing sleeping accommodations for up to six persons; or multifamily dwellings containing two households served through a single meter.

This rate is not available for resale service, multifamily dwellings containing more than two living units served through a single meter or for tourist homes, rooming houses, dormitories, nursing homes and similarly occupied buildings containing sleeping accommodations for more than six persons or for any other Non-Residential usage.

Residences in conjunction with commercial or industrial enterprises and mobile home parks may take service on this rate only under the Rules and Regulations contained in the Company's Gas Rate Book.

Monthly Rate

Customer Charge

$11.75 per customer per month, plus

Income Assistance Service Provision:

When service is supplied to a Principal Residence Customer, where the total household income does not exceed 150% of the Federal Poverty level, verified by confirmation of an authorized State or Federal agency, a credit shall be applied during all billing months.

The monthly credit for the residential Income Assistance Service Provision shall be applied as follows:

Income Assistance Credit: $(11.75) per customer per month

Low Income Assistance Credit ("LIAC") Pilot:

This credit is available for up to 12,000 qualifying Residential customers on a first-come, first-served basis for up to 12 consecutive months. To qualify for the RIA Provision a customer must have been billed $2,500 or less over the last 12 months for gas service and fulfill one of the following requirements:

1. ***Provide evidence of receiving a Home Heating Credit energy draft; or***
2. ***Provide confirmation by an authorized State, Federal or community agency verifying the total household income does not exceed 150% of the poverty level as published by the United States Department of Health and Human Services; or***
3. ***Provide evidence of receiving any one of the following:***
    a. ***Assistance from a state emergency relief program***
    b. ***Food stamps***
    c. ***Medicaid***

The monthly credit for the LIAC Pilot shall be applied as follows:

LIAC: $(30.27) per meter per month, not to exceed the amount of the monthly gas billing for up to 12 consecutive months. Re-enrollment and confirmation of qualification is required for each annual period of participation.

Distribution Charge

$***2.9594*** per Mcf for all Mcf purchased.

Gas Cost Recovery Charge

The gas cost recovery factors are shown on Sheet No. D-2.00.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. D-1.00, surcharges shown on Sheet No. D-1.10, and any applicable charges shown on Sheet No. D-1.20.

Minimum Charge

The minimum charge shall be the customer charge included in the rate.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of transmittal. A late payment charge of 2%, not compounded, of the portion of the bill, net of taxes, shall be assessed to any bill that is delinquent. A customer who participates in the Winter Protection Plan or who is 65 years of age or older and who has notified the Company the customer is 65 years of age or older, shall be exempt from a late payment charge as described in Rule B2, Consumer Standards and Billing Practices for Electric and Gas Residential Service, R 460.122, Allowable Charges.

Term and Form of Contract

Service under this rate shall not require a written contract.

MULTIFAMILY DWELLING SERVICE RATE A-1

Availability

Subject to any restrictions this rate is available to any multifamily dwelling installation containing more than two households served through a single meter and where, in the Company's opinion, it is impractical to provide gas service to each household through an individual meter. This rate is not available for multifamily dwellings containing two households served through a single meter.

Monthly Rate

Customer Charge

The charge per customer per month shall be the sum of the following charges:

$11.75 per month, plus
$0.0715 per Mcf of excess peak demand, plus

Distribution Charge

$***2.9594*** per Mcf for all Mcf purchased.

Gas Cost Recovery Charge

The gas cost recovery factors are shown on Sheet No. D-2.00.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. D-1.00, surcharges shown on Sheet No. D-1.10, and any applicable charges shown on Sheet No. D-1.20.

Minimum Charge

The minimum charge shall be the customer charge included in the rate.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

(Continued on Sheet No. D-10.00)

GENERAL SERVICE RATE
(Rates GS-1, GS-2 and GS-3)

Availability

Subject to any restrictions, this rate is available to any customer desiring gas service for any Non-Residential usage which includes tourist homes, rooming houses, dormitories, nursing homes and similarly occupied buildings containing sleeping accommodations for more than six persons. Gas shall not be purchased under any other rate for any equipment or process which uses gas under this rate.

This rate is not available for residential usage or for resale purposes.

Monthly Rate

	Service Category		
	GS-1	**GS-2**	**GS-3**
***Master* Customer Charge**	$***14.00*** per meter	$***49.00*** per meter	$***669.00*** per meter
Contiguous Customer Charge	***14.00***	***41.95 per meter***	***53.00 per meter***
Distribution Charge	$***2.4763*** per Mcf	$***2.0571*** per Mcf	$***1.3132*** per Mcf

Selection of Service Category and Rates

Customers may choose the Service Category under which they take service, consistent with the provisions of Rules C4.1, Classes of Service, and C4.2, Choice of Rates. When the Customer is selecting its initial Service Category, the Company must advise them that the economic breakeven point between GS-1 and GS-2 is approximately ***1,001*** Mcf per year and the economic breakeven point between GS-2 and GS-3 is approximately ***10,001*** Mcf per year. After the initial selection is made, then it is the customer's responsibility to determine when it is appropriate to switch Service Categories, as permitted by Rule C4.2, Choice of Rates.

Gas Cost Recovery Charge

The gas cost recovery factors are shown on Sheet No. D-2.00.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. D-1.00, surcharges shown on Sheet No. D-1.10, and any applicable charges shown on Sheet No. D-1.20.

Minimum Charge

The minimum charge shall be the customer charge included in the rate.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

Term and Form of Contract

Service under this rate shall not require a written contract.

GENERAL SERVICE OUTDOOR LIGHTING RATE GL

This Rate Is Not Open to New Business

Availability

Subject to any restrictions, this rate is available to any commercial or industrial customer for streetlighting or outdoor area lighting service for any system consisting of two or more gas luminaires where the Company has an existing gas distribution system.

Nature of Service

The customer shall furnish the necessary posts, luminaires and fixtures. The Company shall install this equipment and make all connections to its gas distribution system. The Company shall supply the gas, renew the mantles, clean the luminaires and paint all metal parts as needed; all other renewals and maintenance shall be paid for by the customer.

Monthly Rate

$***7.00*** per luminaire having a rated consumption of 2.5 cubic feet or less per hour.

$***15.00*** per luminaire having a rated consumption of more than 2.5 cubic feet but not more than 4.5 cubic feet per hour.

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. D-1.00, surcharges shown on Sheet No. D-1.10, and any applicable charges shown on Sheet No. D-1.20.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

Term and Form of Contract

Minimum term of three years on written contract and year to year thereafter until terminated by mutual consent or upon three months' written notice given by either party.

Special Terms and Conditions

The Company reserves the right to make special contractual arrangements as to term or duration of contract, termination charges, contributions in aid of construction, monthly charges or other special consideration when the customer requests service, equipment or facilities not normally provided under this rate.

(Continued From Sheet No. E-3.00)

E3. GAS QUALITY (Contd)

E3.2 Heating Value.

The gas transported shall have a total heating value per cubic foot of not less than 965 Btu nor more than 1,110 Btu. Unless otherwise agreed, differences in the thermal value of the gas transported shall be determined by the Company based on the assumption that the gas delivered to the customer has a Btu content per Mcf that is the same as the Company's then-current system average Btu content per Mcf which shall be redetermined monthly.

E4. SERVICE REQUIREMENTS

E4.1 Quantities.

A. The customer may deliver, or cause to be delivered, and the Company shall, subject to other provisions in the Company's Gas Rate Book, accept quantities of gas up to the MDQ specified in the transportation contract. If deliveries to the Company exceed the agreed upon quantities, the Company may terminate the contract upon 30 days' written notice to the customer.

B. Deliveries to the Company may be made by or on behalf of the customer at existing interconnections between the gas transmission facilities of the Company and other pipeline systems. These points of receipt shall be those that are agreed to from time to time by the customer and the Company.

C. The Company shall endeavor to deliver gas to the customer, and the customer shall endeavor to take a quantity of gas that is thermally equivalent to the gas that it delivers or causes to be delivered. Such delivery on the part of the Company and take on the part of the customer is to be made at the outlet of the Company gas meter(s) identified in the transportation contract.

D. The Company shall retain ***2.68*** percent of all gas received from customers being billed for distribution service on the Transportation Service Rate at the points of receipt to compensate it for the Company's use and lost and unaccounted for gas on the Company's system ("Allowance for Use and Loss"). Gas received from customers being billed for distribution services on the General Service Rate shall not be subject to this provision. This volume shall not be included in the quantity available for delivery to the customer.

E. If, in any month, the quantity of gas received by the Company at the points of receipt, less the Allowance for Use and Loss, is more than the quantity of gas taken by the customer at the points of delivery, then the difference shall be retained by the Company and delivered to the customer in those succeeding months when the quantity of gas received by the Company is less than the customer's requirements. Such subsequent deliveries to the customer shall be subject to the withdrawal limitations identified on the Transportation Service Rate Schedule. Should the aggregate quantity of gas, less the Allowance for Use and Loss, retained by the Company at any month-end exceed the authorized tolerance level, then the Company shall have the right: (1) to refuse to receive any additional quantity of gas for that customer until the Company has satisfied itself that the quantity of gas retained for the customer is less than the authorized tolerance level and (2) to assess the customer a Load Balancing Charge for any month-end balance that exceeds the authorized tolerance level.

F. ***After termination of the customer's gas transportation contract, the customer must withdraw or transfer any gas retained by the Company within 60 days. If the customer has not withdrawn or transferred all of the gas retained by the Company within 60 days, the Company will cash out the remaining balance at a rate of $1.00 per Mcf.***

(Continued on Sheet No. E-5.00)

TRANSPORTATION SERVICE RATE
(Rates ST, LT and XLT)

Availability

Subject to any restrictions, service under this Rate Schedule is available to any customer that could otherwise purchase gas under another Company Rate Schedule. A customer selecting transportation service, is not eligible to receive gas under any of the Company's firm gas sales rates for a minimum period of one year from the date the customer commenced taking Transportation Service.

Under this rate schedule, the Company shall transport gas for the customer to the interconnections between the Company's facilities and those of the customer (points of delivery) from the interconnections between the Company's facilities and those of a third party that delivers gas to the Company for redelivery to the customer (points of receipt).

A producer or a broker may contract for service on this Rate Schedule for the transportation of gas from a wellhead through the Company's system to another pipeline, for the transportation of gas from one pipeline to another pipeline or for the transportation of gas from a specified interconnection between the Company's facilities and those of a third party for delivery to a specific customer within the Company's integrated distribution system, provided that all gas transported for a producer or broker pursuant to this Rate Schedule is consumed in and never leaves the State of Michigan after entering the Company's system.

All customers requesting transportation service under this Rate Schedule shall make written application for such service on a form provided by the Company.

Monthly Rate

	Service Category		
	ST	**LT**	**XLT**
***Master* Customer Charge**	$***669.00*** per meter	$***2,216.71*** per meter	$***7491.00*** per meter
Contiguous Customer Charge	***53.00 per meter***	***53.00 per meter***	***53.00 per meter***
Remote Meter Charge	NA	NA	$70.00 per meter
Transportation Rate	$***1.0070*** per Mcf	$***0.8213*** per Mcf	$***0.6930*** per Mcf

Selection of Service Category and Rates

A customer may choose the Service Category under which they take service, consistent with the provisions of Rules C4.1, Classes of Service, and C4.2, Choice of Rates. When the customer is selecting its initial Service Category, the Company must advise them that the economic breakeven point between ST and LT is ***100,000*** Mcf per year and the economic breakeven point between LT and XLT is ***500,000*** Mcf per year. After the initial selection is made, then it is the customer's responsibility to determine when it is appropriate to switch Service Categories, as permitted by Rule C4.2, Choice of Rates.

(Continued on Sheet No. E-12.00)

TRANSPORTATION SERVICE RATE
(Rates ST, LT and XLT)
(Continued From Sheet No. E-11.00)

***Monthly Rate* (Contd)**

Authorized Gas Usage Charge

A customer may request in advance to purchase authorized gas in accordance with the Company's Gas Rate Book. The Company may grant such request if sufficient supplies are available. In such instances, the customer shall be billed for such authorized usage at the customer's Designated Sales Rate, plus $1.00 per Mcf. The customer shall pay $.10 per Mcf for any unused volume that the customer received authorization to take. The Customer Charge shall be that as contained on the customer's designated service category.

Unauthorized Gas Usage Charge

A customer who has not obtained authorized access to the Company's system supply for such Account(s) shall be billed for unauthorized usage at its designated sales rate plus an Unauthorized Gas Usage Charge. Such Unauthorized Gas Usage Charge shall be the highest Midpoint price reported for Michigan or Chicago LDC's during the applicable month as reported by Gas Daily or, in the event that Gas Daily discontinues its reporting of such prices, any comparable reporting service, plus $10 per Mcf for all gas taken by the customer in excess of the cumulative volume delivered to the Company (less gas used by the customer less the Allowance for Use and Loss) on behalf of the customer.

Monthly withdrawals from the customer's previous month-end balance during November through March will be limited to the customer's Contract Storage Quantity (CSQ), if any, plus 3% of the customer's ACQ. If in any month the quantity of gas received by the Company, less the allowance for gas-in-kind plus 3% of the transportation customer's ACQ and its allowed CSQ is less than the quantity of gas taken by the customer at the points of delivery, then the excess delivery will be treated as unauthorized gas usage and subject to the "Unauthorized Gas Usage Charge". For purposes of this calculation, gas transferred to or from another customer during the billing month shall not be considered.

Load Balancing Charge

A customer shall be charged $.25 per MMBtu for any month-end balance of gas that exceeds the sum of its Authorized Tolerance Level (ATL) plus its contract storage quantity. In addition, there is a 2.0 percent gas-in-kind for fuel used for injection, for any month-end balance of gas that exceeds the authorized tolerance level and is in excess of the prior month-end balance.

(Continued on Sheet No. E-13.00)

TRANSPORTATION SERVICE RATE
(Rates ST, LT and XLT)
(Continued From Sheet No. E-12.00)

Monthly Rate **(Contd)**

Load Balancing Charge (Contd)

A customer's ATL shall be 8.5% of the Customer's ACQ unless the customer contracts for a different percent in accordance with the following table. The Transportation Charge shall be adjusted as follows:

Authorized As a % of ACQ Tolerance Level	Transportation Charge Adjustment
6.5%	$***(0.0766)*** Per Mcf
7.5%	$***(0.0383)*** Per Mcf
8.5%	No Change
9.5%	$ ***0.0383*** Per Mcf
10.5%	$ ***0.0766*** Per Mcf

The monthly injection of gas into the customer's ATL and additional CSQ, if any, shall be at the customer's discretion except in September and October when any monthly injections in excess of the customer's CSQ plus 1.43% of the customer's ACQ, will be charged the Load Balancing Charge.

Excess Pipeline Costs Surcharge

This surcharge shall be assessed to the customer.

Due Date and Late Payment Charge

The due date of the customer's bill shall be 21 days from the date of mailing. A late payment charge of 2% of the unpaid balance outstanding, net of taxes, shall be assessed to any bill which is not paid in full on or before the due date shown thereon.

Metering Requirements

All eligible XLT customers shall be required to provide, at no expense to the Company, a dedicated telecommunication line(s) as required for metering purposes, to a location specified by the Company. The communication link must be installed and operating prior to a transportation customer receiving service under Service Category XLT. The customer shall be responsible for (i) ensuring that the communication links allow access to the meter data by the Company and are compatible with the Company's metering and billing systems, and (ii) all associated costs relating to the communication links including other accompanying equipment and monthly fees. The Company shall own and maintain the actual metering equipment and modem.

(Continued on Sheet No. E-14.00)

TRANSPORTATION SERVICE RATE
(Rates ST, LT and XLT)
(Continued From Sheet No. E-13.00)

Monthly Rate **(Contd)**

General Terms and Surcharges

This rate is subject to all general terms and conditions shown on Sheet No. D-1.00, surcharges shown on Sheet No. D-1.10 and any applicable charges shown on Sheet No. D-1.20 of the Company's Gas Rate Book.

Term and Form of Contract

All service under this rate shall require a written contract with a minimum term of one year and month-to-month thereafter which must be approved by an officer of the Company or a duly authorized agent before it shall be binding upon the Company. A customer is eligible to request a return to sales rates 12 months from the date that the customer commenced taking service under the Transportation Service Rate Schedule. A customer requesting a return to sales service must provide the Company with a minimum of 12 months written notice of the customer's intent to return to sales rates. For purpose of the notice requirement, notice must be delivered to and received by the Company. The burden is on the customer to establish that notice has been given. The Company reserves the right to deny return to sales rates subject to the Company's Rule C2, Controlled Service.